FEBRUARY 1956

The Mortgage Banker

MORTGAGE BANKERS ASSOCIATION OF AMERICA MBA ORGANIZED 1914

in this issue

A PLAN TO ACHIEVE STABILITY BY FLEXIBILITY IN FHA AND VA RATES

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MBA 1956 Calendar

February 22, Board of Governors Meeting, Conrad Hilton Hotel, Chicago

February 23 and 24, Midwestern Mortgage Conference, Conrad Hilton Hotel, Chicago

March 12, Mortgage Servicing Clinic, La Salle Hotel, Chicago

March 14, Mortgage Servicing Clinic, Hotel Statler, Washington, D. C.

March 16, Mortgage Servicing Clinic, Andrew Jackson Hotel, Nashville

March 18-20, Southwestern Senior Executives Conference, Southern Methodist University, Dallas

April 5-6, Southeastern Mortgage Clinic, Hotel John Marshall, Richmond

April 7, Board of Governors Meeting, Dinkler-Plaza Hotel, Atlanta

April 9-10, Southern Mortgage Conference, Dinkler-Plaza Hotel, Atlanta

April 30-May 1, Eastern Mortgage Conference, Commodore Hotel, New York

May 10-11, Southwestern Mortgage Clinic, Hilton Hotel, Albuquerque

May 14-15, Western Mortgage Conference, Mark Hopkins Hotel, San Francisco

May 17, Mortgage Servicing Clinic, Olympic Hotel, Seattle

May 18-19, Northwestern Mortgage Clinic, Olympic Hotel, Seattle

June 24-July 7, School of Mortgage Banking, Courses I, II and III, Northwestern University, Chicago

July 29-August 11, School of Mortgage Banking, Courses I and II, Stanford University, Stanford, California

October 8-11, 43rd Annual Convention, Conrad Hilton Hotel, Chicago

The Mortgage Banker

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GEORGE H. KNOTT, *Editor*

Executive and Editorial Office
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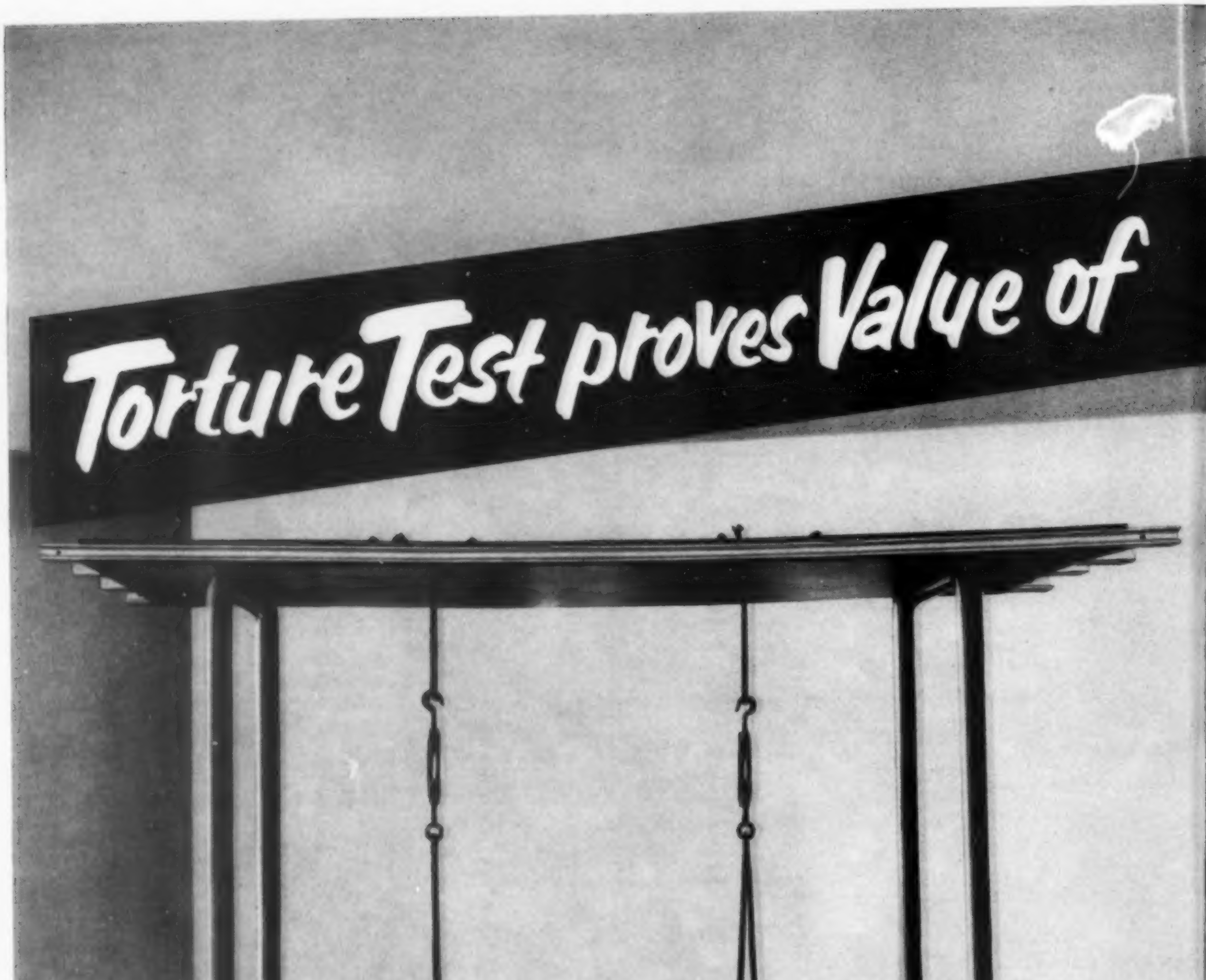
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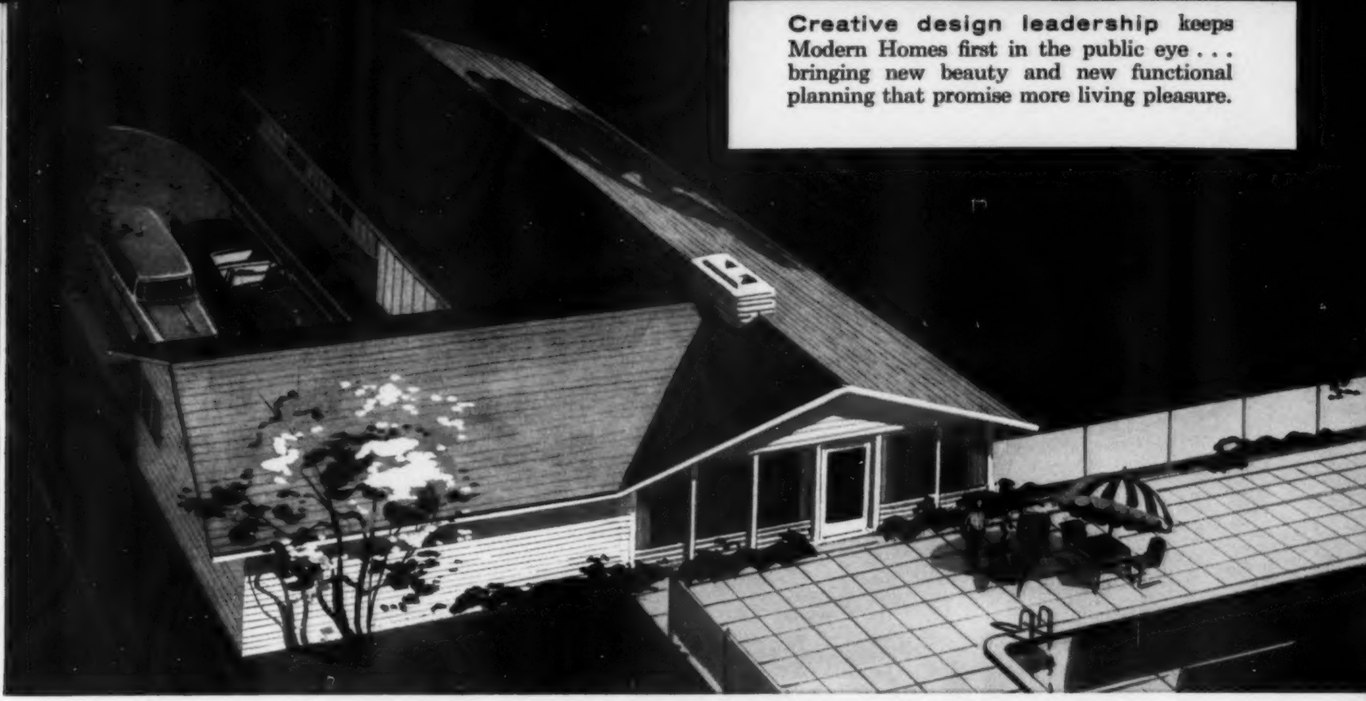

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1956 Could Be
THE PAUSE THAT REFRESHES

Now that all the year-end forecasts for 1956 are in and digested (never before was there such complete agreement in predicting better times ahead), Dr. Nourse has made a critical analysis of conditions as he sees them—and for him the prospects are a little "iffy." Some soft spots exist, particularly in the farm area; but, as he concludes, if we have a pause in the upward movement of recent years it may well be the pause that refreshes for better times later on. Dr. Nourse is with the Joint Council on Economic Education and was formerly chairman of the President's Council of Economic Advisers.

***By* EDWIN G. NOURSE**

THESE projections into the future might appropriately be captioned, "Sober-Reflections of A Superannuated Economist"; and for a crisp summary at the very start, I submit this: In spite of great underlying strength in the economy and obviously unexhausted momentum of general prosperity, I cannot share the easy optimism of those who are already scoring up 1956 as better than, equal to, or at most only a trifle less glorious than 1955. I pinch myself to see if I have just been having a bad dream when I read or hear that there are "no soft spots" in the structure of the boom. On the contrary, I believe 1956 presents an "iffy" situation. Here are a number of the features of the developing economic picture that seem less firmly bottomed than the sure-thing prophets would have us believe—some *ifs* we can ill-afford to overlook.

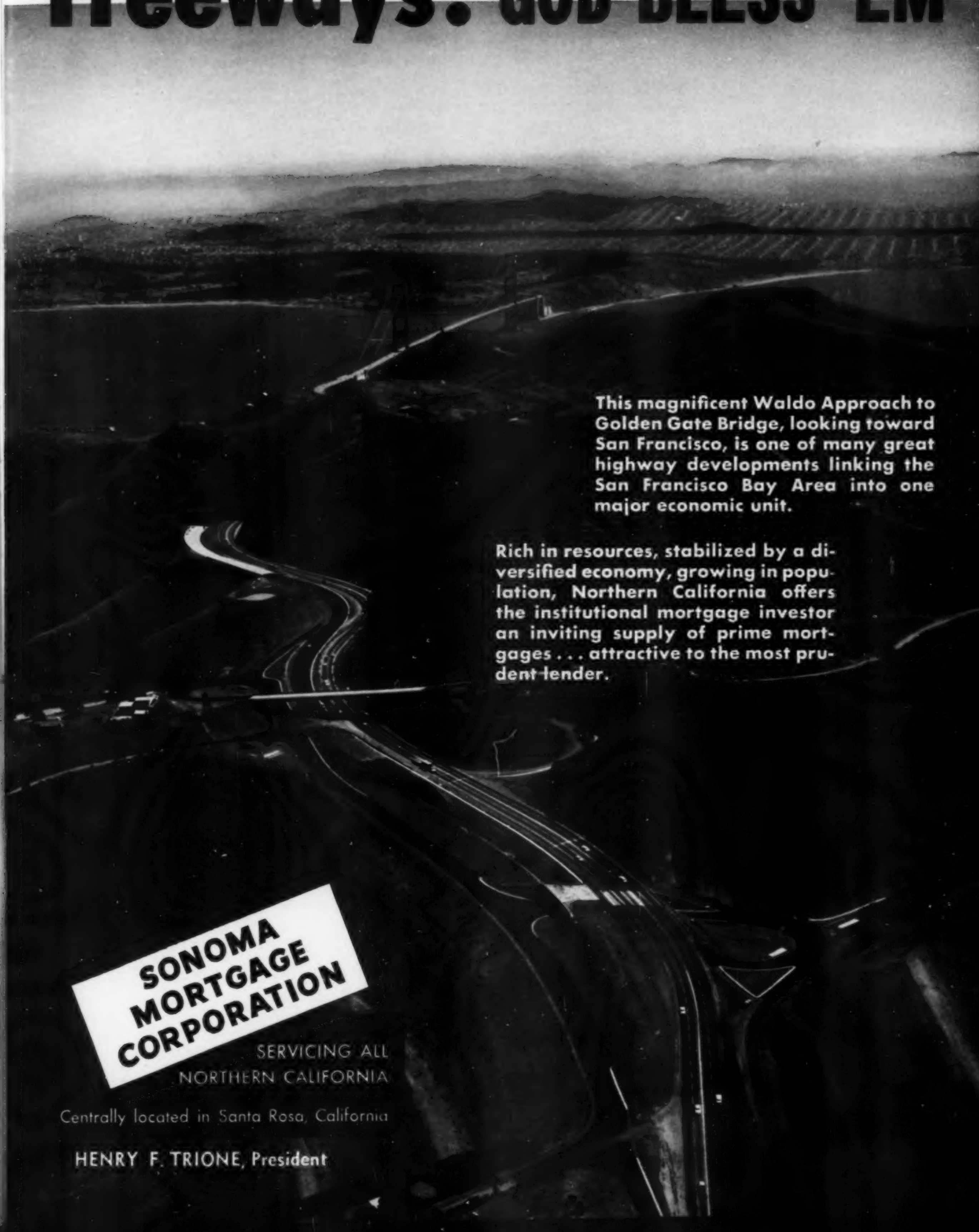
>> FARM: The first soft spot can be disposed of very quickly, though it will be with us for a long time as a headache of the economy and the government. When industrialists and business commentators repeat this "no

soft spots" stereotype, I am moved to wonder whether they are simply ignorant of the facts of rural life or are cynical as to the significance of so great a disparity between one great segment of the economy and all the others. Farm income has been declining steadily and rather sharply for four years, while farm living costs have been rising and bid fair to rise still more next year. Price supports, which served a legitimate and useful purpose in World War II and the Korean affair, were politically extended into the inflationary boom period. There they operated to hoard excess labor on the farms rather than easing the labor shortage in industry, and to drain capital and scarce materials into the production of farm commodities in excess of market capacity to absorb them. More than $7 billion worth of this surplus now overhangs the market, continues to grow $1 billion or more annually under present legislation, and threatens to depress agricultural prices still further in 1956 even if campaign-year legislation does not aggravate the situation further. Assuming average weather conditions and high general prosperity, the Department of Agriculture foresees a decline of some 5 per cent in agricultural income this year. If there should be better-than-average growing conditions and the ebullient consumer market should simmer down somewhat, I would fear a considerable decline in the farmers' ability to buy trucks, tractors, automobiles, fertilizer, and household goods, and a more or less serious chill to be felt in the small-town market for these and other goods. There is basic maladjustment between the agricultural and other sectors of the economy, with powerfully-backed built-in unstabilizers.

>> AUTOMOBILES: It is perhaps a little too much to say "as goes Detroit, so goes the Nation," but any significant change in the tempo of operations in passenger cars, buses, trucks, and tractors is promptly and strongly reflected in steel, rubber, glass, copper, freight traffic, and consumer buying.

For round figures, we may safely call 1955 an 8-million-car year. Until very recently the automobile people have been assuring the public that the worst we need fear as to 1956

Freeways! GOD BLESS 'EM



would be that this year would level off at this high rate before it resumes its triumphal upward march with 9 million cars in 1957. Now they are beginning to concede that it might drop back a little—possibly half a million cars.

The growth line that Mr. Curtice of General Motors foresaw in January, 1955 would not have developed sales of 7.5 million cars until 1956. If we have crowded two years' growth into this one year, it would be easy to see how we might not sell more than 6.4 million cars in 1956. Even that would assume the maintenance of the same level of general prosperity and consumer purchasing power (cash and credit) that obtained last year. But is it to be supposed that those conditions could be fulfilled if activity "at the summit" of our industrial pyramid — the automobile and related industries—were in the process of substantial curtailment of operations? It is worth noting that, even though the 1955 boom was sustained by capacity operation of the autoplants right up through December, with the high level of demand on all their suppliers that that entails, the volume of consumer spending thus engendered was not taking all the cars off the dealers' hands. Inventories began to increase in November, and recent estimates now put them at some 720,000 units. Even remembering that winter is normally a season of accumulation of stocks for the brisker buying season of the spring, this rise in inventories raises the question how long auto plants will keep up their breakneck pace of production in the face of a less-than-expected trend of sales.

» CONSTRUCTION: Some of these internal maladjustments that produce temporary soft spots in what is still global prosperity may be illustrated by construction, and particularly housing. A cheerful way of dismissing any threat of even moderate recession in 1956 is to argue that even if the automobile industry (with its satellites and dependencies) falls off somewhat, the construction industry will fill up the gap and keep the boom rolling at present levels—or better. This is a lovely thought but I venture to advance some sobering reflections.

The construction industry has four

major parts—industrial, commercial, public works, and domestic housing. All these segments show considerable, though varying, strength for 1956. The question is, which one or ones of them will show such expansion above 1955's high levels as to offset the foreseeable weakness in agriculture, automobiles, and other durable consumer goods?

To begin with, we have firm commitments in the way of industrial construction actually under way or in contracts being lost in peak volume from week to week, and in the carefully planned and well-financed construction programs of such large corporations as General Motors, American Tel. & Tel., Du Pont, the big steel companies, and many others. Here we undoubtedly have a strong line of defense against recession getting out of hand following the classical pattern. We may even grant for argument that the total of heavy industrial building in 1956 will substantially exceed last year's and still ask whether that will give any net increase even in the construction industry as a whole. For it is generally conceded that the bottom has already dropped out of apartment house and office building branches, and domestic housing starts have been declining persistently since last May. Neither construction labor nor construction equipment is a fungible commodity, and carpenters, painters, and floor finishers released in the metropolitan East will not be promptly assimilated in building hydroelectric dams or automobile freeways in the West.

Expansions and contractions in the several areas of the construction industry might happily balance each other without contributing any helpful offset to lessened employment and profits in other industries. It remains to be seen how the federal road-building and housing programs that met such an astringent reception in the Congress last year will fare in the present session. But last fall's state and municipal voting showed quite a number of economy straws in the political winds. Disgruntlement over tax burdens and hesitation to raise the ceiling on bonded debt would presumably be still more pronounced if 1956's business activity should show any drop from the boom level of this fall.

In summary, all this thin ice in the

industry picture—construction, automobiles, and other consumer durables —comes down to the "shears" proposition of a no-longer-ravenous demand considerably slacked at the expense of credit commitments enormously expanded. No amount of generalized optimism about our "strong and healthy economy" can remove the need to consider the mechanics of the process by which the complicated cost-price-income relations which have evolved amid the bustling changes of the last few years will work out marketwise and productionwise during the next 12 months.

Turning to the fourth soft spot in the structure of the boom or the fourth area of vulnerability for the economy, we must face the question of how maintenance or enlargement of the boom that some predict would be financed. In the area of credit, there is general agreement as to the importance of the issue and as to the statistical facts. But there is great disagreement as to how the facts are to be interpreted in an appraisal of the economic outlook. This divergence clearly justifies a belief that the situation is indeed "iffy."

On the one hand are those who point with alarm to the risk of commercial bank loans from \$69.4 billion in November 1954 to approximately \$81 billion in November 1955, with installment credit rising from \$22.0 billion to \$27 billion, and mortgage credit rising from \$109.7 billion to \$126.3 billion over the latest reported 12-month. They are concerned about the quality as well as the volume of this credit. On the other hand are those who argue that even though the credit extensions which have been made are large in absolute terms, and have been increasing very rapidly, they are not disproportionate to underlying values or income ratios.

EASY CREDIT

". . . the massive credit extension of 1955 will turn into a neutral or even restraining influence in '56"

My own position does not go either to the extreme of complacent optimism or to the other extreme of fear that this situation is bound to lead to an economic crash. The point which seems to me of vital significance is that liberal extensions of credit on private mortgages, business loans, and consumer durables was used as a prop to the continuance and enlargement of the boom throughout 1955. It has gone to the point where Federal Reserve and other authorities have applied successive restraints and where a few outspoken bankers have referred to credit terms as "fantastic."

To give the devil his due, let us assume that every credit extension was justified by the underlying security and that every loan will prove self-liquidating within its original time limit or with extensions which can be easily borne by the lenders. The point that is significant for 1956 is that the effort of borrowers to validate all this outstanding credit on the terms just described will mean that earning power of many individuals and firms must be thriftily husbanded to the meeting of these credit obligations. This will inevitably constrict their ability to make new purchases in 1956 and dampen their willingness to take on new credit commitments. If, at the same time, automobile and other payrolls are reduced even moderately and company profits are less lush than they have been this year, buyer caution would become still more pronounced. The stimulus which has been furnished by the massive credit extensions of 1955 will turn into a neutral or even restraining influence in '56 as payments of interest and curtailment of principal impose a prior claim on disposable income of the debtor.

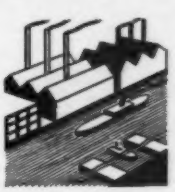
Both business officials and private individuals have had a long conditioning to prosperity and economic expansion—15 years or more. Not only has this decade and a half had the negative effect of wiping from their minds the fear of any considerable recession, but also, on the positive side, they can point to two recent downturns which have been held to

the most modest proportions, after which the economy promptly bounced back to renewed and accelerated prosperity. This strongly fosters the belief that "it ain't gonna rain no more." But I share the view of my distinguished successor in the Council of Economic Advisers, Arthur Burns, that it will take a much longer historic record of economic stability to justify faith that the business cycle is dead or has been overcome—however much its pattern may have changed.

Faith in a continued boom through 1956 seems to me often to be resting on an inordinate confidence in projection and expectations techniques. These are good tools of economic analysis in the hands of experts but misleading or dangerous unless the assumptions on which they are based and the qualifications with which they are accompanied are kept in full view. It is an almost universal human failing to assume that a present condition or a recent trend is going to continue. In particular, it is very easy to rationalize optimism at the height of a boom.

Consumers undoubtedly had fun spending as lavishly as they did in 1955 and would like to continue on this plane in 1956. But when they respond to the poll-takers' questions they have a tacit assumption: "If my income keeps up to its present level (or prospects of improvement) and if I keep my present health and

INDUSTRY'S BOOM



"It is very easy to rationalize optimism at the height of a boom."

tastes, I'll probably spend and save on about this pattern." But loss of overtime, the furloughing of one member of the family earner group, or even uncertainty in one community because of lay-offs in another, or rumors of lay-offs makes yesterday's expectations as dead as yesterday's newspaper.

I mentioned the implicit faith that many forecasters place in the investment pronouncements of prominent companies in the flush of prosperity. But the Voice of Experience should remind us that such plans inevitably undergo an agonizing reappraisal when sales shrink, inventories pile up, and uncertainty clouds the business sky. It would not strain the memory to recall 1949, when outlays for plant and equipment dropped to a $17.8 billion rate (seasonally adjusted) in the fourth quarter from a $22.3 billion rate in the like quarter of 1948 (and back to $23.3 at the end of 1950).

Of course, the degree of clarity and rationality of spending plans and their makers' ability to implement them varies widely. Small companies do not have either liquid resources or the courage to persevere in carrying out long-range plans through periods of temporary uncertainty as do the giants whose expansion plans have been given so much publicity. And

even the big boys can, without actually abandoning or even permanently curtailing a project, slow down its timetable. And this is even more true of the durable consumers' goods and the thick fringe of services that enter into the household budgets of our well-paid middle class — which should perhaps now be called the "model class." From the situation of 1945 with its enormous backlog of unfilled wants, a decade of high production has brought us to the point where the consuming public is loaded with postponables. I cannot dismiss the possibility that a drop of even 2 per cent in jobs this year would cause the actual spendings both of consumers and business to fall substantially below the expectations expressed in the latest expectations surveys.

Finally, the political underpinnings of the recent boom and the political vulnerability of business in 1956 are obvious. Purged of all partisanship stands the objective fact that the boom of the last three years has been in no small degree powered by confidence in the present Administration as "creating an atmosphere favorable to business." Uncertainty as to the continuance of this Administration and this atmosphere is already evident, and political uncertainties of one sort and another will continue and perhaps increase as the campaign progresses. I do not see how this can fail to cumulate with other unsettling or deterrent forces in 1956 business.

In summary, the general characterization of 1956 seems to me to be too good to be true. I see more likelihood of the traditional saw-tooth formation, in which boom forces that mount slowly on the upside break with much more speed on the downside.

This does not mean crash and depression. Our accumulated resources, our improved institutions, and our enlarged economic sophistication safeguard us against that menace. The situation is much like the mili-

tary developments after the breakthrough in Normandy. A wide advance went far and fast. Some units overshot their objectives: some drives were stopped or driven back; logistics became strained. In time there had to be a pause for rectifying the general line: re-grouping, replacing, and re-equipping for a new advance. In such a process some untenable positions have to be abandoned and some plans revised, but the shift is accomplished—in the military—within a tight system of command and discipline, for which we have no counterpart in a free enterprise economy. The alternative we have is business intelligence, personal fortitude, and mutual forebearance.

These qualities will meet a real test in 1956. We should contemplate a possible drop of 15 or even 20 per cent. Only so shall we be prepared to meet what we may have to meet. We should not be too sure we can get away with it as 5-per-centers. We should not count on the magic of "built-in stabilizers" because some things so labelled are built-in unstabilizers. Nor should we suppose that the controlling or compensating action of monetary and fiscal policy will fully protect businessmen, labor, and consumers from their lack of prudence in the flush of prosperity or their lack of fortitude or daring in the pinch of recession. Government's arsenal of weapons to combat recession, though impressive, is still untried in any full sense. Private adjustments must be our main reliance, merely backstopped by government policy.

Thus conceived, the disinflationary recession of 1956 can be simply "the pause that refreshes."

Life insurance purchases were at new peak levels in English-speaking countries in 1955, running as high as 20 per cent more than the year before.

Preliminary reports indicate the following increases: Australia 20 per cent; United Kingdom 12 per cent; Canada 5 per cent; United States 4 per cent. Excluding Federal Employee Group Insurance for both years, the U. S. gain was 18 per cent.

» **PROTECTION:** About one-third of the nation's employed civilian work force is now covered by some form of pension plan. The majority of these workers are also covered by Social Security.

It is estimated that some 22,000,000 persons are enrolled under pension plans, almost one-fifth of them under plans insured by life companies.

Private pension plans of all types account for over 60 per cent of the total number of these persons; state, county, municipal or federal civil service plans for 20 per cent; the balance being railroad employees or persons under profit-sharing plans with some retirement feature.

The greatest rate of growth has been in the private pension plans, those covered by such plans having more than doubled in the past ten years and now numbering five times the number reported in 1935.

From the best estimates available, it appears that the number of workers covered by pension plans of all types, private and public has increased by almost 350 per cent since 1935.

Private pension plans have shown the greatest percentage increases in these years. The number of private pension plans in force rose from 1,090 in 1935 to 7,425 in 1945 and no less than 20,000 in 1955, at least a twenty fold increase for the 20-year period. The number of persons covered by these private plans has grown from 2,600,000 in 1935 to 5,600,000 in 1945 and nearly 14,000,000 at the start of 1955, an increase of more than 400 per cent for the 20 years. Of the nearly 14,000,000 covered last year, 1,000,000 were actual pensioners under private plans.

» **4 ANNIVERSARIES:** Since MBA has experienced its greatest growth in the past decade, it follows that most firms now holding membership have joined during that period. Consequently, not every member is aware that in the Chicago and Washington offices are people whose connection with MBA goes back further than the membership of most members today. Secretary George H. Patterson is celebrating his 25th year with the Association, an event which was suitably recognized at the last annual Convention with the award of a plaque calling him the country's Mr. Mortgage Banker.

Frank J. McCabe, Jr., assistant secretary and treasurer, is celebrating his tenth anniversary. He began as director of education and research and grew up with this phase of MBA's activities. The largest part of the development of MBA's educational program—second to none in the country among trade groups—took place under his direction.

Samuel E. Neel, MBA general counsel, is also rounding out ten years

with MBA in 1956. About the same kind of tribute can be paid him—practically all of MBA's work in the national capital has occurred under his direction. And it has been a busy decade in that department, too, with a different look. The staff was Secretary Patterson, himself and two secretaries, and the entire office was little larger than the secretary's own office today. Regional meetings had not been started, there was no regular

George H. Patterson

Frank J. McCabe, Jr.

Samuel E. Neel

George H. Knott

each passing year presenting new legislative problems for consideration and solution, to say nothing of the day-to-day servicing chores which are laid before him.

This year is the twentieth anniversary for George H. Knott, editor of *The Mortgage Banker*, public relations executive and director of various other duties. When he came with MBA, the Association did indeed have Washington representation, no educational program, no permanent servicing department. FHA had just emerged, and, to say the least, there was mixed feelings about it. The mortgage industry is a big business today, an important wheel in the economic machine; but a very large part of it has developed within the service of those now on the MBA national staff.

The Investment Climate Ten Years from Now

By O. Kelley Anderson
President, New England Mutual Life Insurance Company

While most lenders and investors are finding it difficult enough to gauge investment conditions of the last half of this year, Mr. Anderson takes a flyer at forecasting what we may reasonably expect during the next ten years. Assets of life companies will practically double, amounting to around $180 billion. Will there be a demand for all these savings? He's emphatic on that point—there will be. "Ten years from now we will not have to scratch around very often to find places to put our policyholders' money." In Mr. Anderson's view, a busy, useful decade looms ahead.

WHAT will the investment climate in 1965 be like? First, I will drop the basic requirements of a life insurance investment man—those of prudence and conservatism—and indulge in speculation. One can't be dogmatic that far ahead in investments with any precision — so it is necessary to speculate.

O. Kelley Anderson

As an indication of how speculative one must be, recall what someone might have said in previous decades with respect to the future investment climate.

In 1945 speculation on the future would have been replete with defeatism. At that time, refundings at lower rates of return were rampant, the Department of Commerce conservatively estimated an unemployment pool of 10 million men due to demobilization, and excess manufacturing capacity due to war needs would eliminate major capital demands for years—reorientation to economic normalcy would take 10 years.

In 1935 speculation in the future on an optimistic basis would have been rank heresy. We were at an investment impasse—there were no new frontiers—over-saving had ruined normal business, our investment departments were running real estate offices, reorganizations, and bondholders committees—former giltedged securities were contributing to the cost of life insurance in reverse.

In 1925 there was pie in the sky, golf in the afternoon, and men were enviously eyeing the rarified easy life of the management team in the home office's senior echelon.

No wonder a guess into 1965 must be rank speculation! Of course, if I were speculating for 2,005, I would have much more leeway. Few would be around to second guess, and those who were would probably be traveling to the moon to look over the equity holdings in the variable annuity account. The trip would probably be made in a flying saucer which had just been fully amortized on a purchase and lease-back.

But to examine the investment climate in 1965, here are two assumptions.

First, that we will have a dynamic and relatively healthy economy; and, *second,* that we will have no shooting war and if we do have a continuation of the Cold War, its significance on our economy will not be relatively greater than it is at the moment. Obviously, any predictions would be worthless if we are drawn into a full-scale war.

Now speculating ahead, what will the assets of the life insurance industry be in 1965? How much money will we have to invest annually, and will we be able to put all this money to work at satisfactory rates?

The assets of all U. S. life companies will practically double during the next decade and by 1965 will amount to at least $180 billion. This estimate is a conservative one, based on an annual growth of 7 per cent, which is somewhat lower than the rate prevailing for the past several

years. Some may wish to challenge the optimism of this rate, since there is at the moment some concern about the effect of term and group sales on the industry's financial growth. On the other hand, however, most of us have erred on the downside, and the growth of nearly every segment of the economy has rather consistently exceeded our expectations.

This same projection shows that our assets will increase by $12 billion in 1965. As a rough rule of thumb, we can "guesstimate" that our cash flow at that time will range somewhere between 1⅔ and 2 times our estimated growth of assets. This means that we will have a cash flow of somewhere between $20 and $24 billion. Personally, I believe it will be closer to $24 billion—because I am sure that our holdings of industrial direct placements and commercial mortgages will be greater 10 years from now. These investments, with their higher and accelerated amortization, can make the estimate of $24 billion a reality. These billions will be in competition with the other billions of institutionalized savings. This poses the obvious question—will there be enough demand for this money 10 years from now?

I say "Yes," for the people, living in an economic climate of confidence, will create the necessary demand for capital. With the American public's constant drive for an ever-increasing standard of living, with its demand for new and improved goods and services, we will have no problem finding suitable investments.

First, the most dramatic demand for capital will come from American business through the billions it is spending annually on research. In turn, this research creates demand for both men and money to develop the resulting new products. It is commonly considered by people engaged in research and engineering that for each $10 spent on research, one of those dollars will result in a new or improved product. For each of those dollars, it requires $10 of capital to develop the product in a pilot plant, and $100 of capital to create the production plant. Last year alone, $4 billion went into research which will ultimately create a $48 billion capital demand for pilot and production facilities—not to mention the additional billions which will be required for working capital purposes. The most dynamic factor affecting the future of life company investment portfolios is the present-day research of American industry. I don't think we can in any way overexaggerate the importance of this research which was sparked and accelerated during the recent war years.

"If I am at all right in my belief that demand for capital will exceed the available volume of savings in the decade ahead, then I wonder if we have adapted some of our investment policies to this situation. For example, in a lender's market, why should we continue to offer borrowers such attractive terms in regard to prepayment provisions? Why should we give the borrower the option to pay off our loans at a slight premium whenever interest rates may have temporarily declined? I haven't heard anyone suggest that the borrower should give us an option to raise our interest charges on an existing loan whenever interest rates in general rise—I am sure most borrowers would be horrified at any such idea! Yet we give the borrower an option which in effect says, heads he wins, if interest rates decline; and tails we lose, if interest rates rise."

Second, we cannot escape the fact that the United States has become the world's financial center. I am confident that, barring war, American capital is going to flow in large and increasing amounts to foreign countries. How it will be done and what mechanisms will be used I don't know, but the basic facts are inescapable. Foreign nations, and particularly those that are undeveloped, are in desperate need of capital to develop their natural resources; and to satisfy the growing aspirations of their people for a better standard of living. In fact, the demands are so great that rates of interest and profit potentialities are being offered which dwarf anything that we consider at all normal in our own country.

Of course the risks are great, but if the United States is to fulfill its role as the financial capital of the world, as the only country which has financial resources large enough to meet these foreign demands, American investors and American entrepreneurs are going to use their ingenuity and find ways to do the job. Any way you look at it, this is going to be an important factor in determining the volume of funds that will be available for investment within our own country. It seems to me that the life insurance business will sooner or later be forced to gain a better understanding of what is going on in the financial and industrial world outside of our borders. Whether or not the life insurance business will participate directly or indirectly in foreign financing, I have no idea as of now. All I am saying is that this foreign demand for capital is going to be satisfied; it is going to be satisfied largely by American capital, it is going to influence our domestic financial picture, and we should lose no time in improving our knowledge of what is really going on in this exciting new era of foreign development.

In addition to the foreign demands for capital, there will be a big domestic demand for toll roads, public construction and schools. Recently the Chase Manhattan Bank stated that it would cost $101 billion to put our highway system in adequate shape by 1965. If we think we are building a lot of roads now, it may be surprising to know that, per vehicle mile, we are putting only about one-half as much money into highways as we did during the 1920's. And how about the new capital that will be needed to supply gasoline, tires, steel, and aluminum for the 30 to 35 million additional cars and trucks which will be on the road in 1965!

We still have tremendous sums to spend for financing our increased elementary and high school popula-

tion. In addition, by 1965 our college enrollment will be almost twice as large as it was in 1954. Our basic plant requirements for education during the next 10 years may be running into multi-billions of dollars — not multi-millions. Capital for these plants will have to be supplied by someone and will reduce the amount of savings available for other purposes.

I believe we can look forward to one thing with confidence—the demand for capital will continue to be large. I am completely sure that 10 years from now we will not have to scratch around very often to find places to put our policyholders' money. I think our problem as an industry and as a nation is going to be to find enough savings to finance the things that can and should be done.

Whether we like it or not, government influence on and over business seems to be here to stay. We have had a revolution in political thinking that is not confined to any single political party. It finds expression in such laws as the Employment Act, Minimum Wage Acts, Social Security, governmental protection of the bargaining position of labor, and in the government's relation to agriculture. Whether the enlarged role of government in our economy is wise or not is not important; and whether we like it or not is now beside the point. The fact is that government does play a large role in our economy which is broadly supported by the voting public.

Many of these acts, together with other machinery the government has set up, provide an under pinning of protection against serious declines in our economy. Although these so-called stabilizers do provide a prop to the economy, we will know more definitely by 1965 whether the government can control major economic fluctuations. These controls would appear to primarily forestall recessions. Whether the government is in a position to control inflationary excesses is still a speculation.

Still on the government area, I doubt if any administration during the next 10 years will resort to the deficit financing policies of the Roosevelt and Truman Administrations. I cannot, therefore, anticipate any great changes in the volume of government debt—and as a result, I believe that governments will show a relative decline in life company portfolios. The big problem confronting the Treasury is to lengthen the maturities of the government debt. We in life insurance have a moral obligation to assist them with their task; and I am convinced that by so doing, we will be serving the best economic interests of our policyholders. Whenever necessary, we should act as underwriters to insure the success of the government's refinancing program. I am not, however, implying that it is mandatory that we become long-term holders of government securities.

Looking ahead ten years, it seems inescapable that life insurance companies, as well as other investors, are going to be called upon to look into new types of investment and into business and industries which will be technically far more complicated than what we are accustomed to deal with today. It is not so many years back when life insurance investing was a comparatively simple matter, consisting for the most part of conventional real estate mortgages and underlying bonds of governmental units, the railroads and the public utilities. Large investment staffs were not needed and finance committee meetings were comparatively stereotyped.

The railroads have ceased to be important consumers of the kind of credit which we can supply. While the public utilities are still taking a significant part of our funds, the dramatic changes of the past few years have centered chiefly in the financing of industry and trade. This has required expansion of our investment staffs and the employment of more and more specialists whose task it is to keep abreast of technical and other developments in a host of business enterprises. It has required increasing ingenuity to find specific financing mechanisms to meet specific situations. It has included the development of so-called direct placements, of purchase lease-backs, not only of real estate but more recently of equipment itself. We have also seen the development of new wrinkles in indentures which were unheard of years ago.

We in life insurance must put increasing emphasis on building up our investment departments. We must attract the best available men; and we must remember that in this area of the life insurance business, we can afford nothing less than the best in talent, experience and judgment. We have superior investment talent now, but our problem of building in this area in 1965 will be unusually important.

If I am at all right in my belief that demand for capital will exceed the available volume of savings in the decade ahead, then I wonder if we have adapted some of our investment policies to this situation. For example, in a lender's market, why should we continue to offer borrowers such attractive terms in regard to prepay-

(Continued on page 37)

"Whether we like it or not, government influence on and over business seems to be here to stay. We have had a revolution in political thinking that is not confined to any single political party. Whether the enlarged role of government in our economy is wise or not is not important; and whether we like it or not is now beside the point. The fact is that government does play a large role in our economy which is broadly supported by the voting public."

Are We Heading for Trouble?

By E. SHERMAN ADAMS
Deputy Manager of ABA's Department of Monetary Policy

Trouble? Who's thinking about trouble—trouble when a new year has opened more auspiciously than almost any other within memory. Why not continue to enjoy the comforting glow that comes from prosperity unbounded, prosperity such as no other people have ever known before? Indeed, why not? No reason except that it might be wise to take a look at the other side of the coin—just to see what's there. Is it the same? Well, not quite.

The boom has been a durable goods boom, and it's been accompanied by an enormous increase in debt—"never before have so many" owed so much. But savings have increased enormously too—yes, but, fact is, not as fast as personal incomes. Money supply? It's been expanding since 1949 but what is more important is its velocity, its turn-over—that has been increasing faster. And so on and on. In most of the principal areas from where we derive our business optimism, there is another interpretation of the facts when you examine them coldly and realistically, as Dr. Adams does here. He is predicting no bust—nothing even close to it. What he does contend is that many things the country has been doing for the past decade cannot go on forever and he hopes we will be able to adjust to a new set of conditions with as little disruption as possible.

MANY thoughtful people today are wondering how long this prosperity of ours can continue. We see houses, automobiles, and appliances of all kinds being produced in profusion and sold on terms that seem, in some cases, fantastic. We see people spending freely and going more deeply into debt. And in the background, the stock market has been zooming toward the stratosphere.

Dr. E. S. Adams

Is this rather hectic prosperity sound and enduring? Or is it flimsy—based too much on borrowing and other stimulants? Will the boom level off nicely into a period of stable growth? Or will there be trouble?

Our wives have a gift for phrasing the problem more dramatically, something like this: "People are spending like mad. Everybody is living on the down-payment. Everything seems to be on paper. How long can this thing go on?"

These misgivings are in sharp contrast with the happy-go-lucky optimism among some people. Now, as always during a boom, we have with us prophets of perpetual prosperity. Industry, they say, is making giant strides into a new era—this time the real thing, atom-powered and jet-propelled—and nothing can possibly go wrong.

But to many, these glib assurances are not reassuring. Indeed, they are disturbingly reminiscent of 1929. Our economy has been boiling along now without much interruption for more than 15 years, the biggest boom in our history; and we know that in the past, booms have always sooner or later come to an end.

A collapse of the 1929 variety? None fears another holocaust like that. Our economy is structurally far more stable than it used to be. Our banking system is in strong condition. We have an impressive array of safeguards against adversity—the farm support program, unemployment insurance, lay-off payments, and the like. Government has assumed responsibility to help stabilize the economy, and we have a better understanding of how monetary and fiscal policies can be used effectively.

These considerations rule out a deep and prolonged depression. But they do not necessarily rule out a decline larger than the gentle dips of 1949 and 1954—something more nearly comparable perhaps with 1937-38 when stock prices declined 25 per cent, industrial production slid 20 per cent, and unemployment increased by 3½ million. No, we are not worrying about another 1929; but we do wonder whether a fairly serious recession may be in the making.

Some people are blithely happy about the future because they are so impressed by the enormous growth that lies ahead for the American economy. They seem to be hypnotized by projections of the vast markets that should exist by 1965 or 1970.

All of us are aware of the future promise of the American economy. What is more, we can be confident that our strong growth factors—and the anticipation of growth—will help to sustain economic activity over the years ahead.

On the other hand, we know that the mere existence of a big growth potential does not guarantee stability. After all, we had big growth potentials in 1920 and in 1929 too. Indeed, our entire history has been one of

remarkable growth which has been interrupted from time to time by serious setbacks. We are still left with the question as to whether we are now heading for such a setback.

To answer this question, we need to analyze what has been going on in our economy during the past six years. The decade of the 40's was dominated by the effects of World War II. By the end of 1949, however, we appeared to have become fairly well adjusted to these wartime influences, partly through expanded production and partly through higher prices.

In examining our economy today, therefore, we should regard what happened during the 40's as being largely ancient history. In 1950 we started to write a new chapter in our economic history. What concerns us now is how this new chapter is going to turn out.

During the first phase of this new chapter, the economy was stimulated by the Korean War and the rearmament build-up. Now, after a brief readjustment in 1954, we have moved into a new phase, consisting of an old-fashioned peacetime boom. These two phases have much in common. Many trends have continued with little interruption since the new chapter began in 1950. It is clear that, as of today, the forces operating throughout the past six years have not worked themselves out in the form of a stable, well balanced economy.

Looking at the record of these six years, we can see that economic expansion has received its chief impetus from the exceptionally high production of durable goods — plant and equipment, housing, automobiles and the like. It is true that an expanding economy needs large quantities of durable goods. It is also true that vacancy rates are still low in many localities, that there is a strong movement to suburban areas, and that there is a marked trend toward putting two cars into every garage—if you can squeeze them in. New patterns of living have been emerging; and it may well be that with the rapid growth of the middle-income group, the markets for housing and for automobiles have taken on new and much greater dimensions.

But the question remains: Is the durable goods boom *durable?* This question cannot be answered by pointing to unfilled needs for housing or to the public's passion for more cars and for more car per car. The durable goods section of our economy has always been a volatile one. Perhaps it has become less volatile now than formerly, but should we assume that it can now go only upward—and steadily?

The fact stands out that the durable goods boom of the past six years has been accompanied by a huge expansion of debt. The rise in public borrowing, including state and municipal obligations, has not geen great; but private indebtedness has expanded by almost $160 billion—an enormous increase.

The key factor in this picture has been a phenomenal rise in personal indebtedness, namely, consumer credit and residential mortgages. Since the end of 1949, consumer credit has increased by $17 billion or 100 per cent; and personal mortgage debt has increased $47 billion or 126 per cent. Total personal indebtedness has risen about $65 billion or 118 per cent. Never before have so many owed so much more so fast. This inflation of personal debt has been responsible for a large part of the expansion of borrowing by business concerns.

The real import of this rapid increase in personal indebtedness does not seem to be widely understood. A whole array of arguments has been advanced for being complacent about it; such as: (1) that it has been accompanied by a large volume of personal savings, (2) that it has not caused a huge expansion of the money supply, (3) that it has not resulted in overall price inflation, and (4) that the present level of personal debt is not dangerously high.

First, let's take the savings picture. It is true that since 1950 personal savings have been fairly large. However, savings are normally large during a boom—for example, 1927-29—and they have not proven to be the stabilizing factor that some people assume.

During the past six years, most savings dollars have been channelled into the durable goods industries (including the construction industry) and have stimulated this volatile part of the economy. Dollars injected into these industries probably have a higher rate of turnover, a higher multiplier effect, than they would ordinarily have. Also, rapid expansion in these industries has resulted in substantial wage increases, and it so happens that wages in these industries tend to set a pattern for others.

Can our people pay their debts? In Adams' opinion, the "crucial point is this: regardless of whether personal debt is now 'too high,' its rate of increase in recent years cannot possibly continue forever. No one can say just how long this rate of increase might be maintained—perhaps for a number of years but sooner or later it inevitably must slacken. When that happens there are bound to be repercussions in the durable goods industries and throughout the economy. To put it differently, our present prosperity has been powered by an increase in personal borrowing at a rate that cannot be sustained indefinitely. The question is how serious the shock to our economy will be when this rapid inflation of personal debt decelerates."

Moreover, personal savings since 1950 have not risen as fast as personal incomes. In fact, for the past several years, personal savings have been declining not only in relation to personal incomes but even in dollar amount. Recently, demands for credit have been running far ahead of the supply of savings.

Second, the money supply. There has been a considerable increase in the money supply—demand deposits plus currency—since the end of 1949; but, if looked at by itself, the expansion has not been alarming. But the point is that money supply should not be looked at by itself. We cannot ignore the factor of velocity, the rate at which money has been turning over.

When we do take into account this factor of velocity, the picture looks quite different. While the money supply has been expanding fairly rapidly since 1949, its rate of turnover has also been increasing and very appreciably. Recently the turnover of demand deposits in leading cities outside New York has been averaging more than 25 per cent higher than it averaged during 1947-49.

So when we put the factors of money supply and money turnover together, they multiply out to a very substantial monetary expansion over the past six years. Not only are there more dollars, but most dollars are being handed around faster, being made to do more work. For example, manufacturing corporations are today doing about 35 per cent more business per dollar of cash on hand than they did during 1947-49.

All this suggests that too much attention may have been given to the volume of money and not enough to its velocity. A moderate increase in the money supply should not be regarded with complacency when money velocity is rising rapidly at the same time.

For instance, some observers seem to derive great comfort from the fact that the increase in bank loans last year was largely offset by a reduction in bank holdings of government securities. As a result of these divergent influences on the volume of bank deposits, money supply did not show an extraordinary increase for the year.

However, some of the government securities sold by the banks were purchased with funds otherwise idle, whereas most of the dollars that were borrowed have been quickly put to work. This is reflected in the sharp rise in the velocity figures.

If these points seem rather academic, recall that the situation during 1927-29 was in some respects parallel. During that period, the boom in durable goods and the stock market inflation were financed not by an expansion of the money supply but by an increase in the velocity of money turnover.

"Somewhere along the road we are going to have to do some adjusting. If we use restraint and common sense, there is no reason this cannot be done. Perhaps there is some danger of slowing down too fast, but there would probably be greater danger in further sustaining trends and thereby risking worse trouble later."

Some people dismiss these considerations as being theoretical. They point triumphantly to the comparative stability of overall price indexes since 1951 as proof positive that nothing can be seriously wrong. This argument also calls for analysis.

It is misleading to talk about prices since 1951 without looking back a little further. After the Korean outbreak in June of 1950, some sensitive prices shot up rapidly and subsequently reacted to somewhat lower levels. Other slower-moving prices began to advance and have continued to rise ever since without much interruption. For proper perspective on the price situation today, the price inflation since June, 1950, should be taken into account.

Moreover, a big reason for the overall stability of prices over the past few years is that agriculture has still been in process of adjusting to postwar conditions. Declines in agricultural prices have masked the strong upward trend in many other prices. Sooner or later, farm prices will stop declining. When that happens, the inflationary trends in other parts of the economy will be more evident in the general price level.

Overall price stability since 1951 has therefore reflected a continuance of inflationary pressures. Otherwise, more prices would have receded when the shortages after Korea were overcome. It should be remembered, too, that price movements in recent years have adversely affected many people —not just farmers and home buyers, to cite obvious examples—but millions of others as well.

The steadiness of the overall price level since 1951 has tended to hide imbalances in our economy, notably the debt-financed boom in durable goods. Again there is a similarity to the late 1920's. Then as now the stability of prices was widely cited as a reason for confidence. In retrospect, it seems clear that the price stability of the 20's concealed the development of unstabilizing trends in the economy.

We have now reached the stage in the present boom where, unless its pace abates, the pressure on prices will increase. During a large part of the past two years, this pressure has been alleviated by the fact that we have had some slack in the economy. Now that this slack has been taken up, the situation is quite different. This has been clearly evidenced in recent months by increasing shortages and price advances for more and more products.

In short, the present period of expansion has not been by any means devoid of inflationary elements, as some people seem to assume. Now that we are operating at full capacity, inflationary pressures are becoming intensified.

Now we come to the argument that personal indebtedness is not dangerously high at the present time. It is pointed out that people's incomes have risen substantially and that their debts are not excessive when related to personal disposable income, or especially if related to so-called discretionary income.

Now this question of whether personal debt has now become "too high" is one that can be argued indefinitely. From the standpoint of the future stability of the economy, it is not the main point at issue.

The crucial point is this: regardless of whether personal debt is now "too high," its rate of increase in recent

years cannot possibly continue forever. No one can say just how long this rate of increase might be maintained — perhaps for a number of years—but sooner or later it inevitably must slacken. When that happens, there are bound to be repercussions in the durable goods industries and throughout the economy.

To put it differently, our present prosperity has been powered by an increase in personal borrowing at a rate that cannot be sustained indefinitely. The question is how serious the shock to our economy will be when this rapid inflation of personal debt decelerates.

The answer will depend on three factors: (1) on the abruptness with which this shift occurs, (2) on what is done to cushion its impact, and (3) on whether it is aggravated by other unstabilizing developments.

As to the first of these factors, the longer the rapid increase in personal debt continues, the more abrupt the eventual change is likely to be. Also, the longer it continues, the greater the danger that other imbalances may develop. It would be less disruptive to have some slow-down in debt expansion now while our economy is in generally strong condition than to have an abrupt change later on when our economic health may be less vigorous. The sooner debt expansion slows down to a more reasonable pace, the better.

Will we achieve a fairly orderly transition to a slower rate of debt expansion that will sustain prosperity and growth but will not be inflationary? There are some indications that we may. In the field of mortgage credit, inflationary tendencies have recently shown some abatement. As for instalment credit, it is contended by some that the stimulus provided by the easing of terms is now about over. In the case of both of these types of debt, the rising volume of repayments will tend to slow down the growth of the totals.

In addition, the Federal Reserve's policy of monetary restraint has helped to dampen inflationary pressures. Whenever the inflationists step up their criticism of the Federal Reserve, you can be pretty sure that our credit control machinery is operating as it should to combat inflation. We can be quite confident that it will continue to be helpful over the period ahead.

Some observers believe that monetary policy combined with the self-correcting tendencies at work in both mortgage and instalment credit will suffice to bring about a fairly satisfactory balance in the economy in the not-too-distant future. They may be right; and all of us, certainly, hope they will turn out to be.

But they could be wrong. We know from experience that self-correcting tendencies are not always reliable, to put it mildly. Moreover, even the most skillful monetary policy cannot assure economic stability. Indeed, we may be in danger of placing too much faith in what the Federal Reserve can accomplish.

"Our economy has been on a bit of a spree. So far the party has not gotten very wild. If we taper off fairly soon, we should be in good condition tomorrow. But if we prolong the party and keep on having just one more for the road, the after-effects may be very unpleasant."

One limitation of Federal Reserve policy is that it operates primarily through its effects upon the banking system, whereas most personal credit is extended by nonbank lenders. Consequently, the influence of Federal Reserve policy on personal indebtedness is largely indirect, delayed and uncertain. This being the case, monetary policy should not be regarded as a precise and efficient weapon for dealing with the present situation.

Much will depend, too, upon what is done to cushion the adjustment to a slower rate of debt expansion. As this adjustment proceeds, there will undoubtedly be pressures for the application of stimulants — demands for tax reductions and for increased government spending and stimulation of residential construction. Also, if business recedes, Federal Reserve policy will doubtless shift in the direction of ease.

Now it may well be that some stimulants will be desirable during the adjustment period. However, if stimulants are carried too far, we may whirl off on a new extension of the boom, and one more inflationary than the present phase. This would mean building up to worse trouble later on.

If the boom does continue for a while, various excesses could develop which might lead to trouble. One danger is the possibility of inventory speculation, which has frequently accentuated the fluctuations in our economy. As yet, there has been little evidence that business inventory policies are becoming speculative. This still could happen, however, especially if there are increasing signs of shortages and higher prices.

Unwise policies with respect to wages could also have a seriously unstabilizing influence. Available evidence suggests that wage increases over the past year may have exceeded the average increase in productivity. Too rapid wage increases could undermine economic stability and complicate the problems of the readjustment period.

The stock market is another potential danger spot. It has caused trouble in the past and could again. Much of the market rise since 1942 has been justified by the higher price level, the plowing back of corporate earnings, and the enlarged productive and earning capacity of American industry. The market today is not floating on a sea of credit as it was in 1929. With margin requirements now subject to regulation, it is less explosive than it used to be.

Nevertheless, even if the market is not fantastically high, it is certainly in very high ground and the possibility of a substantial break cannot be ruled out, especially if prices go much higher. Such a decline would undoubtedly have a depressing effect on spending both by business and by many individuals.

Excesses in any of these areas could have serious consequences, especially if they were to occur in several areas at the same time.

What *can* we conclude? First, it seems clear that some unstabilizing trends have developed in our economy. Now that our productive resources are being strained to capacity, the problems created by these trends are becoming more acute.

(Continued page 38)

Stability Can Be Achieved Th

WHEN the U. S. Treasury needs to raise money through borrowing, it makes a careful study of the bond market and then offers a new issue at an interest rate and for a term of years which it believes the market will absorb at par. Such flexibility in terms and interest rate means that the government bond market, at least with reference to new issues, enjoys a degree of stability that is seldom true of the market for *newly-created* FHA and VA mortgages.

J. M. Pringle

Just as you never hear of the U .S. Treasury making a new offering of treasury bonds at a discount, so the market for new conventional first mortgages is practically always a par market. For the purposes of this discussion, it is still, to all intents and purposes, a par market even when the borrower pays an origination fee or when, in a particularly easy money market, the lender pays a finder's fee or small premium. There is, of course, nothing stable about the money market and so how is it possible to achieve this price stability for new conventional mortgages? The answer is obvious—by *flexible* interest rates. When money is tight, borrowers giving conventional mortgages as security must pay a higher rate of interest and conversely when money is easy and lenders are competing for conventional mortgages, they do so by offering borrowers a lower rate of interest.

Stability is achieved through flexibility.

In the highly important field of FHA insured and VA guaranteed mortgages, market stability for newly-created mortgages is sadly lacking and the main reason, it seems to me, is that with interest rates set by Congress, the law of supply and demand (which even Congress can't repeal) exerts its influence on *price* rather than on interest rates. The result is the kind of premium or discount market that we have experienced most of the time since the end of World War II. When insured and guaranteed mortgages sold at substantial premiums, as they did for some years during and after the war, the mortgage banker and/or his builder client pocketed an extra profit which they did not deserve. That, in my judgment, contributed to inflation and certainly was not good for the economy as a whole. In recent years, as all of us in the mortgage business know full well, new VA and FHA mortgages have quite consistently sold at substantial discounts and there seems little doubt that a large part of this extra cost of financing has been passed along to the home buyer, through higher prices than would otherwise have been necessary, or in the case of rental housing to the tenants through higher rents.

Is it possible to achieve what, in my opinion, would be an ideal situation where newly-created FHA and VA mortgages fluctuate in price only between say 98½ and 101½ which could be considered virtually a par market? I think so but only if a way is found to take the fixing of FHA and VA interest rates "out of politics." Perhaps that one condition makes it impossible after all! Even so, let's tackle it. Fair heart never won fair lady nor persuaded politicians to disregard the demagogic appeal for votes implicit in a low interest rate for the "little fellow."

It is, of course, true that the government, either by new legislation or by new regulations of the FHA and VA, does change from time to time the maximum interest rates that may be charged for VA and FHA loans. Unfortunately such changes have been made quite infrequently and have not reflected the ups and downs of the sensitive market for government bonds. Two years ago I suggested that Victory 2½'s of 1972-67 be used as an index and that whenever the yield obtainable from these bonds advanced by ¼ of 1 per cent, the VA and FHA should be *required* to increase their interest rates by the same amount and, of course, to decrease them when the money market moves the other way.

One major problem is to determine what is the "right" differential between the yields obtainable for government insured and guaranteed mortgages, after allowing ½ of 1 per cent for servicing, and from government bonds. My suggestion two years ago was that when Victory 2½'s gave a yield of 2.75 per cent, the VA and FHA interest rate should be 4½ per cent producing, after ½ per cent servicing, a 4 per cent net yield or 1.25 per cent more than the Victory 2½'s.

However, the mortgage market of the last two years would seem to indicate that a better index might be the Treasury 3's of 1995 now selling to yield a little less than 3 per cent and that the differential between these bonds and say minimum down payment maximum term VA mortgages should be 1.50 per cent, not 1.25 per cent. Currently such 4½ per cent VA loans are selling at 96 to yield 4.48 per cent, after ½ per cent servicing. In figuring this yield, I have ued a 30 year mortgage but have assumed that on the average such mortgages will be prepaid in 12 years. In order for such mortgages to sell at par in the current market, it's obvious that the interest rate would have to be 5 per cent.

Our formula could then be that when the longest term governments sell to yield 3 per cent, the least desirable (maximum term minimum down payment) VA and FHA mortgages should carry an interest rate of 5 per cent. Then, should the yield from the longest term governments advance to 3.25 per cent, and stay there for ten consecutive business days, the VA and FHA interest rates for minimum type loans would automatically be increased to 5¼ per cent or on the other hand if the yield from the longest term governments should decline to 2.75 per cent and remain

Through Mandatory Flexibility of FHA and VA Interest Rates

By J. MAXWELL PRINGLE

"I feel very strongly," says Mr. Pringle in submitting the proposal he does here, "that the housing laws, as passed by Congress, and as administered by such agencies as VA and FHA, should have as their objective the establishment of a flexible interest rate pattern designed to make newly-originated VA and FHA mortgages command a market price in the 3 point range from $98\frac{1}{2}$ to $101\frac{1}{2}$ . . . there is general agreement that the present situation, where newly-created FHA and VA mortgages immediately sell at large discounts, is bad for the economy, as a whole, and particularly bad for buyers of small homes . . ." There's a precedent for doing exactly what Mr. Pringle proposes — in the debentures which FHA issues for defaulted loans.

The logic of the reasoning back of his proposal is sure to interest lenders and investors and stimulate some thinking on the subject. Mr. Pringle is president of Pringle-Hurd & Co., Inc., of New York and well known in the mortgage industry.

at that level or lower for ten consecutive business days, the VA and FHA interest rates would automatically be reduced to $4\frac{3}{4}$ per cent.

It is interesting to note that a precedent has been set with reference to flexible interest rates. I refer to that part of the 1954 housing law which provides for flexibility, based on a formula, for the interest rates carried by government guaranteed debentures issued in connection with defaulted FHA insured mortgages. Such debentures, with 20 year maturities, issued with respect to any mortgage insured on or after August 2, 1954, are required to bear interest at the debenture rate which was in effect at the time the mortgage was insured. The debenture rate during the latter part of 1954 was set at $2\frac{1}{2}$ per cent but with the approval of the Treasury Department, FHA has the authority to establish the debenture interest rate at any future time in an amount not in excess of the annual rate of interest determined by the Treasury, estimating the average yield to maturity on the basis of daily closing market bid quotations or prices during the calendar month next preceding the establishment of such rate of interest, on all outstanding marketable obligations of the United States having a maturity date of 15 years or more, from the first day of such next preceding month and by adjusting such estimated average annual yield to the nearest $\frac{1}{8}$ of 1 per cent. It seems evident that the FHA considers that the housing act not only gives them the authority to make such changes in the debenture interest rate but also that they are, in fact, obligated to make such changes unless the Treasury Department disapproves. At any rate, on January 1, 1955, the debenture interest rate was advanced from $2\frac{1}{2}$ per cent to $2\frac{5}{8}$ per cent and on July 1, 1955, it was advanced again to $2\frac{7}{8}$ per cent.

It is interesting that this sound principle of flexibility of interest rates has been followed in the relatively unimportant field of the government guaranteed debentures issued in connection with defaulted FHA insured mortgages. There are two reasons why the interest rate on FHA debentures is of very minor importance. First, considerably less than 1 per cent of all FHA insured mortgages have terminated in default and so relatively small amounts of FHA debentures have been issued. The second reason is that the date which governs the interest rate on FHA debentures is not the date of default when the debentures are issued but the date that the defaulted mortgage was originally insured. For example, if a mortgage was originated during the latter part of 1954, when the FHA debenture rate was fixed at $2\frac{1}{2}$ per cent, the holder of that mortgage, in the event of a default during the early part of 1956, would receive a 20 year FHA debenture at $2\frac{1}{2}$ per cent even though the FHA debenture rate for loans insured at this time would be $2\frac{7}{8}$ per cent. It seems to me that the principle of adjusting FHA debenture interest rates to conform with the government bond market is a good one but would be more equitable to holders of mortgages if the interest rate was determined by the rate in effect at the time the debentures are issued rather than the rate in effect at the time that the mortgage was insured. Over a period of years the changes in interest rates would average out and I don't believe that the percentages of defaults on FHA mortgages would be very much greater during periods of high interest rates than when interest rates were lower.

However, while the matter of the interest rate on FHA debentures issued only when FHA loans default is, for the reasons already set forth, relatively unimportant, I do consider it

most important that Congress recognized, in passing the 1954 housing act, that flexibility in interest rates based on a formula is desirable. Certainly if it is desirable with reference to FHA debentures, it is very much more desirable in connection with the VA and FHA interest rates on the mortgages themselves. Quite possibly instead of adopting a new formula along the lines suggested earlier, it would be a good idea to urge that Congress use, for adjusting FHA and VA interest rates, exactly the same formula that is now being used for the relatively minor matter of adjusting the FHA debenture interest rate. The law could provide that VA and FHA interest rates for minimum down payment maximum term loans must be changed up or down with every change of ⅛ of 1 per cent in the average yield available from all government bond issues having a maturity of 15 years or more. In my judgment, the differential between this government bond average yield and the interest rate on the least desirable FHA and VA mortgages should be 2 per cent. After allowing for ½ of 1 per cent servicing, this would mean that FHA and VA mortgages at par would yield 1.50 per cent more than the average yield obtainable from all government bond issues having maturities of 15 years or more. At the present time the FHA debenture interest rate is 2⅞ per cent. Consequently, if this suggestion were enacted into law, the FHA and VA interest rate would now be set at 4⅞ per cent.

Objection will undoubtedly be made in some quarters that to change the interest rate on mortgages ⅛ of 1 per cent at a time would result in too frequent changes. I will admit that it hasn't been customary to change mortgage interest rates by ⅛ of 1 per cent, but all lending institutions, in buying bonds, are accustomed to coupon rates expressed in eighths and I see no reason why to quote mortgage rates in terms of eighths should not be acceptable, particularly when applied to mortgages backed by government insurance or guarantees. Certainly variation by eighths would give even greater assurance of a stable market around par for newly originated FHA and VA mortgages.

It should be kept in mind that the kind of flexible interest rates suggested here would be designed to make the *least desirable* VA and FHA mortgages sell close to par at the time of origination. I believe it would also be most advisable to have flexibility based on the quality of the loans. Probably the only effective test of quality would be the amount of down payments and the terms of the mortgage. While I realize that there are other tests of quality, such as location, type of construction, etc., it would be difficult to apply such tests on a national basis. Let's assume that 30 year, no-down payment VA loans would carry, at the present time, the maximum interest rate of 4⅞ per cent. I would suggest that where the borrowers' down payment ranged from 5 to 10 per cent, the maximum interest rate be decreased to 4¾ per cent, that with down payments ranging from 10 to 15 per cent, the maximum interest rate be fixed at 4⅝ per cent, that loans having down payments of 15 per cent to 20 per cent carry an interest rate of 4½ per cent and that in all cases where the borrowers are able and willing to pay down more than 20 per cent, the interest rate be fixed at 4⅜ per cent. Such a flexible interest scale based on down payments would give the veteran borrower a powerful incentive to make such down payments. Furthermore, in my judgment, quality loans at rates lower than the maximum would, in all probability, be considered worth around par by many selective lenders. The law could provide for similar reductions in interest rates for quality FHA loans—in other words, loans where the mortgagor's equity is more than the minimum required by the FHA and the term of the loan is less than the maximum permitted. It is interesting that in a very minor way the FHA has long recognized that some loans are more attractive to lending institutions than others and that the least attractive loans should, therefore, carry a higher interest rate. I refer particularly to the old Title I Section 8 loans—now known as 203i's—where the borrower not only pays 4½ per cent interest, but in addition pays ½

of 1 per cent service charge. The interest rate on such loans is, in effect, 5 per cent.

To summarize, I feel very strongly that the housing laws, as passed by Congress, and as administered by such agencies as VA and FHA, should have as their objective the establishment of a flexible interest rate pattern designed to make newly originated VA and FHA mortgages command a market price in the 3 point range from $98\frac{1}{2}$ to $101\frac{1}{2}$. I fully realize, however, that no legislation of this kind could be drafted, enacted and administered with any assurance that it would fully accomplish this objective. Consequently, if after a year's trial it could be shown that price fluctuations, except in isolated cases, exceeded this 3 point range, the basic law could be amended either with reference to the index (formula), the differential or both. I do consider it important that the basic law *require* that the VA and FHA make automatic changes in mortgage interest rates based on a specific formula and, of course, the formula itself should be changed only when it can be demonstrated that a basic change has taken place in the overall relationship between the government bond market and the FHA and VA mortgage market. Quite probably in war times or other national emergency, the President should have the right to direct the VA and FHA not to make interest rate changes without first securing his approval.

I think there is general agreement that the present situation, where newly-created FHA and VA mortgages immediately sell at large discounts, is bad for the economy, as a whole, and particularly bad for the buyers of small homes who must, in the long run, pay higher prices in order to offset the builder's substantial extra financing cost. It's also bad for a great many builders not lucky enough or smart enough to be able to pass these extra costs along to the ultimate consumer. Quite possibly a few of the lending institutions are content with the present large discount market but I'm certain that the majority of all lenders would much rather buy a 5 per cent mortgage at par than a $4\frac{1}{2}$ per cent mortgage at 96. It should not be forgotten that sooner or later the pendulum will swing the other way and then if interest rates remain relatively fixed, mortgages, when scarce, will again sell at premiums. That, in my opinion, is almost as bad for the economy as a discount market. Theoretically, such a situation can be corrected by originating VA and FHA mortgages at less than the maximum rate or rates permitted by the FHA and VA but in actual practice, this has seldom been done in the past. The reason is a selfish one. Mortgage originators and/or their builder clients thrive on a premium market for government insured and guaranteed mortgages and welcome the windfall profits that rightly belong to home owners in the form of lower interest rates.

Mandatory flexibility of interest rates is the answer. Only in that way can stability be achieved and inflationary trends curbed.

INVESTMENTS IN 10 YEARS

(Continued from page 29)

ment provisions? Why should we give the borrower the option to pay off our loans at a slight premium whenever interest rates may have temporarily declined?

I haven't heard anyone suggest that the borrower should give us an option to raise our interest charges on an existing loan whenever interest rates in general rise—I am sure most borrowers would be horrified at any such idea! Yet we give the borrower an option which in effect says, heads he wins, if interest rates decline; and tails we lose, if interest rates rise.

In a period of high corporate income taxes when the tendency is for corporations to borrow fully rather than to raise additional equity, is there anything improper in suggesting that at least part of the proposed debt should give the lender some opportunity to share in the profits made possible by that part of the loan which really represents at least a semi-equity position?

Although I would like to, I am not going to get into the subject of increased investment by life companies in common stock equities. It does seem clear, however, that the attitude toward common stocks has changed profoundly in the last ten years, and I suspect it is likely to change still further toward a more

liberal use of investment funds through this medium. Dr. Fabricant of NYU believes that the price level is likely to be higher in 1965 than it is now. By the same token, it must necessarily mean that our unit costs of conducting the life insurance business will rise also. Equity investment in reasonable amounts gives some opportunity to hedge against this possibility of rising costs, and of keeping the net cost of insurance to the minimum. We all know that there may have to be changes in the investment statutes of some of the states if equity investments are to be increased. Massachusetts has had a very liberal attitude toward equities ever since the prudent man rule was adopted back in 1830. My own company bought its first stock nearly 111 years ago. I think a lot of other States would do well to follow Massachusetts' example. There are serious and difficult problems involved in how common stocks should be valued for balance sheet purposes; but they are not unsurmountable problems by any means.

One of the difficulties in pursuing a flexible and progressive investment program geared to the investment requirements of business has to do with our investment statutes. Great progress has been made in revisions, but unfortunately most of the revisions have been aimed to meet a specific situation, and as a general proposition these investment statute changes have come only after a considerable time lag. Perhaps we should give greater consideration to giving statutory freedom for managerial decisions on investment matters through basket provisions permitting part of the assets to be invested in any way not strictly forbidden by law.

In 1965 our investment man with billions of dollars to invest, and the high level of capital demand, will be screening hundreds of new industries and thousands of new products. They will be open minded and flexible in their thinking, putting more and more of their faith in the people who will be managing the enterprises of the country. Operating under more liberal, and I hope more uniform investment statutes—with more attractive interest rates — they will be making, as they are today, a major contribution to our over-all earnings and to the low cost of insurance.

HEADING FOR TROUBLE?

(Continued from page 33)

Somewhere along the road we are going to have to do some adjusting. It remains to be seen whether we will adjust smoothly. If we use restraint and common sense, there is no reason why this cannot be done. Perhaps there is some danger of slowing down too fast, but there would probably be greater danger in further sustaining unsustainable trends and thereby risking worse trouble later.

Our economy has been on a bit of a spree. So far the party has not gotten very wild. It we taper off fairly soon, we should be in good condition tomorrow. But if we prolong the party and keep on having just one more for the road, the aftereffects may be very unpleasant.

Perhaps we should look at our economy in broader perspective. All of us are aware of the tremendous achievements of American industry.

As for the future, we are clearly confronted with enormous opportunities. In these United States, we are actually well on our way toward the abolition of poverty, that age-old curse of man. Over the decades ahead, if we keep our economy functioning properly, we can further improve the living standards of all Americans and greatly raise our standards of health and education. This is our vision for the future. It is up to us to make it come true.

Aubrey M. Costa Is Head of Dallas MBA

Aubrey M. Costa, president, Southern Trust & Mortgage Co., Dallas, and former MBA president, has been elected president of the Dallas MBA, succeeding James A. Cheek of the W. A. McKinley Co. Glenn Justice, president, Glenn Justice Mortgage Company, Inc., was elected vice president, and Jerry B. Frey, Jr. of Brown-Frey Mortgage Company, was re-elected secretary-treasurer. This Association now has 65 members representing 52 life companies, banks and mortgage and trust companies.

President's Page

NINETEEN fifty-five was a year to remember in mortgage banking—it would appear that more people in the industry did more business than in any previous year in history. Now, with the first month of the new year underway, what are the prospects for 1956? My observations lead me to the conclusion that it will be another excellent year for our industry, possibly with a volume of recordings not quite up to last year's and with housing starts of around 1,100,000—but still a productive and profitable year to contemplate.

Lindell Peterson

Money will continue tight, demands for credit from all users of capital will be heavy and with interest rates probably remaining at about at their present levels—with little possibility of a marked change either way. A return to the excessively easy credit conditions of recent years (despite the return of 30-year loans) is out of the question.

All in all—as I pointed out to members of the New Orleans and Chicago MBAs in recent addresses at their meetings—it should be a good year for mortgage lenders, builders and, particularly, home buyers. A little of the exuberance will be missing but a more substantial performance can be anticipated.

And certainly the year promises to be a useful and productive one for MBA. The program which your Association has underway to benefit its members is such that your trade organization is a partner in your business more than ever before. Within the space limitations of this page, I would like to mention some of the principal projects in work.

Since one of the most valuable aspects of an association is the opportunity for those within its industry to gather and explore their mutual problems, MBA this year is providing these facilities on a nation-wide basis as never before—major Mortgage Conferences in Chicago, New York, San Francisco and Atlanta and Mortgage Clinics in Richmond, Albuquerque and Seattle. About everything that concerns us as mortgage men will be authoritatively covered at these meetings. The more you can attend, the more you will profit.

Our educational program, one of MBA's greatest achievements, is being further expanded. Course III is being added to the Northwestern University School of Mortgage Banking, thus completing the curriculum, and Course II is being added at the Stanford School. Our MBA-NYU Senior Executives Course this year had twice the applicants it could accommodate; now we are adding a Senior Course at Southern Methodist University in Dallas. The program will be available soon and it will be a rewarding experience for any member. The course for Business School Deans and staff members at the University of Michigan last year produced constructive results and will be given again in 1956, but at a different college, possibly the University of Colorado.

Something entirely new has been added to MBA activities—one-day Clinics in Chicago, Washington, D. C., Nashville and Seattle in March devoted to nothing but servicing. These will prove profitable for any member but particularly for personnel in the accounting and servicing departments. I suggest that you be sure to send some of your staff to these Clinics—they will profit but your business will gain most.

Our legislative committee has been streamlined to function more efficiently. The chairmen of the GI and FHA committees have been named vice chairmen of the legislative committee. A new subcommittee has been organized to undertake a most important assignment for the Association: a study of obsolete state laws governing mortgage investments, foreclosure provisions and loan-to-value ratios. Our public relations committee is exploring ways to better acquaint the public with the role and functions of the mortgage banker in our economy.

A special liaison committee is being organized to work in closer cooperation with other contemporary associations regarding matters in which we have mutual interests. Our research program has a wide list of projects under way. One is a study of the possibilities of developing a system whereby several investors would subscribe to a joint audit of a correspondent, thus eliminating duplication. Another is a study of how mortgage bankers can render better service to the public. Still another is a factual inquiry into mortgage yields vs. bond yields.

This year will be a busy one for the country and a busy one for MBA. The objectives are high and their attainment will depend, as has always been true in the past, on the interest and cooperation of the Association's members.

Lindell Peterson

PRESIDENT

Voice of the Home Office

There's a Broad Field for Improvement In Investor-Correspondent Relations

One medium-sized mortgage company told the author that between 20 and 25 auditors had gone over its books during the course of a year. But many investors, because of the size of their portfolios and costs involved, make no audit of their correspondents at all. There are two extremes in investor-correspondent relationships. Mr. Shugrue asks whether it might be possible for the life companies to set up some kind of central audit bureau available to all participating companies. It's one of the thoughts—and there are others equally worth thinking about—which Mr. Shugrue sets forth in this discussion of mortgage correspondents, investors and appraisers. These pages are usually devoted to unsigned contributions of investors and correspondents airing their views of any and all things that pertain to both of them. Because what Mr. Shugrue has to say here is so applicable to both the lender and originator, both departments this month are being devoted to his views.

By FRANK R. SHUGRUE

Second Vice President, Bankers Life Insurance Company of Nebraska

BECAUSE of the great expansion in mortgage activity in recent years, I think it would be expedient for life companies to review their mortgage operations, examine their practices, look into their relationship with their correspondents, glance at their appraisal requirements and scrutinize the rules under which they operate. Recently, before preparing a speech before the American Life Convention, I wanted to get the benefit of current thinking in the mortgage industry and some idea of appraisal problems; consequently I wrote to a number of leading mortgage bankers and talked to many prominent appraisers from all sections of the country. I inquired what they had to criticize and what they had to suggest to institutional investors. My observations here, of course, are greatly colored by these replies.

In the mortgage industry there is considerable sentiment that the inauguration of the amortized mortgage was the greatest phenomenon since the invention of the wheel, that the amortized mortgage is the sole reason for the remarkably low delinquency experience now being enjoyed. There is little doubt but that monthly payments on principal, interest, taxes, insurance and special assessments has vastly improved the attractiveness of the mortgage as an investment; it is not, however, a panacea. There is still ample room for improvement in the industry. Much could be done for further progress through a closer liaison between the life insurance industry, the Mortgage Bankers Association of America and the American Institute of Real Estate Appraisers.

When we consider the archaic laws which are the rules under which life insurance operates, we realize that a thorough study is called for. Little consideration has been given to the changing economy and living habits that constitute America today. Legislation covering mortgages was enacted, for the most part, with an agricultural economy in mind. Few will dispute the fact that the income derived to make payments on farm loans is different from that which services the debt on a city property. I have no quarrel with the latitude allowed the farmer under many present foreclosure laws. Shorter foreclosure periods, as applied to city properties, would result in even fewer delinquencies than now exist for in a credit economy mortgagors soon learn that the payments can be made first on the television set or on the washing machine or on the car because it takes so long to get into trouble on a mort-

Voice of the Correspondent

gage default. Many states which are now feeling a dearth of capital would find much more money available if a mortgagee did not have to go through a long costly procedure in order to protect his investment.

The laws which authorize mortgage investments make no distinction with regard to the hazard an investor may have in protecting his investment. It does not seem probable that a company has the same risk when it makes a two-thirds loan in a state where it can be in title within 60 days after default as it has when it makes a loan in a jurisdiction where it takes 2 to 2½ years to accomplish the same result. The difference in the time required to complete the foreclosure can make a tremendous difference in the real estate market.

Would it not be reasonable then to allow an investor to make a 75 per cent loan where the asset behind the security can be had in 60 days? Or would it not be expedient to require a much lower ratio loan in an area which necessitates 18 to 24 months to do the same job? If this difference in authorizing the investment were made, states would modernize their laws in order to attract capital. We may or may not agree that the New Jersey law allowing 75 per cent mortgages on fully amortized deals with special reserves for the overage is good, but it at least indicates that changes can be accomplished and that progress can be made in securing a review of mortgage laws. Undoubtedly, any changes of this nature must be accomplished at the local level but methods and procedures could come from a national organization level.

If we in life insurance were to ask the correspondent and the investor what facet of the mortgage business presented the greatest problem, the answer would probably be the "in and out" situation which has been the result of the extraordinary activity in mortgage lending during the past few years. The investor would say that this situation is necessary to a certain degree because of the difficulty in estimating cash flow and the supply of mortgages offered. The correspondent would counter with the statement that the origination of mortgages cannot be turned on and off like a water faucet. This problem presents a real challenge at both levels.

No Over-the-Transom Loans

Relatively few mortgagors walk into a correspondent's office and apply for a loan. More often than not, the application submitted to an investor is the result of considerable "bush beating" by a solicitor. In originating the application he may have contacted an architect who gave his client's name to several mortgage solicitors. He may have gotten the lead from a builder. He may have been following the transfer of lots in a desirable area and called a new lot purchaser. He may have followed a surveyor's truck to see what lots were being surveyed for new homes or possibly a real estate broker told him that he had made a sale. In any case, when the contact was made with the applicant a certain plan must have been offered, an amount of loan estimated, a rate quoted, and financing costs figured. These estimates must have been made with an investor's program in mind.

Before an application results the applicant has probably talked to two or three other mortgage people including a savings and loan association and probably a bank. If our solicitor gets the application, processing starts. An appraisal must be made, credit information secured, pictures taken and various forms filled out. Then it must be sent off to the investor for further processing. More often than not the time which has elapsed between first contact and actual submission may be a week or two. This is a conventional loan. It is not difficult to understand the correspondent's reaction when he receives a letter from his investor which states that the loan appears to be satisfactory but that he is out of the market.

This situation is no exaggeration. It has occurred many times. It has happened when, at the same time, an investor has been purchasing blocks of loans in the area serviced by the correspondent. Investors expect loyalty from their correspondents. Correspondents are a necessary part of the team. It is incumbent to give the same loyalty which they expect. But under some circumstances it is just about impossible to avoid a withdrawal from the market. The tremendous surge of applications during the early part of last year upset the most careful calculations. This period saw an increase of mortgage debt to $82.5 billion on 1-4 family non-farm dwellings, an increase of $12.8 billion in one year. Changes in fiscal policies of the Federal Reserve Bank and of the treasury department cannot be foreseen and incorporated into investment planning particularly mortgage investment planning. Nevertheless, each investor owes his correspondents the time it takes to hesitate and plan a program, to estimate the runoffs, to gauge the amount of new money which will be available for investment and to determine how the money is to be invested. If it is decided that some percentage of these funds are to be put into mortgages, they should be allotted to faithful correspondents on some reasonable basis. When withdrawal from the market is indicated, ample notice should be given to the correspondent so that processing can be stopped at the "retail" level.

These observations about planning investments may seem fundamental. They are. Nevertheless, I know of instances where investors have no pro-

gram whatever. Mortgage bankers are urged to set up an origination program only to be cut off in the middle, without any warning whatsoever. This is not sound. It hurts everyone involved.

Seldom Seen Investors

People associated with the mortgage industry have one common objective in mind, to improve the attractiveness of the mortgage as an investment. One way to accomplish this end is to cut the costs inherent in handling mortgages. Lower costs mean higher yields. This is axiomatic. During recent inspection trips I have inquired of many mortgage bankers as to the number of auditors that visit their offices during the course of a year to check their books for their investors. The number surprised me. One medium-sized company indicated that between 20 and 25 auditors had gone over their books during the course of the year. Because of the small size of the portfolio and the cost involved, many small companies make no audit of their correspondents whatever. It appears to me that we have unnecessary duplication at one extreme and unwarranted risk at the other. Would it not make sense to have a central audit bureau of some sort sponsored by our industry with services available to all? Any company doing business with a correspondent could then subscribe for audit service on a pro-rata cost basis. For instance, companies A, B, C, D and E have a common correspondent. The bureau does an audit of the correspondent periodically and bills each investor for its pro-rata share of the cost. Such a system would enable smaller companies to get a much needed service and larger companies should experience lower costs. Net result: higher yields and better protection for investors as a whole with much less office interruption for the correspondent.

During the past few years we have been hearing a great deal about the "single debit" system of mortgage accounting. Some astounding claims have been made for its great reductions in home office costs. If the cuts in cost claimed are anywhere near correct, it deserves some study. When inaugurated, the idea met with strong objection at the correspondent level because it obviously increases the correspondent's burden to some degree. However, after a trial period it is surprising how the reaction mellows. I recall having heard a correspondent voicing terrific objection when he was forced to adopt the system by one of his major accounts. Now, less than two years later, he thinks it is the finest thing that could have happened. He has discovered that there has been very little increase in his costs and that he has quick internal control never before enjoyed. It appears that the single debit system requires periodic audit of the correspondent by the investor. My purpose in mentioning the single debit method is to illustrate how its use could be more readily considered by the smaller company if reasonable audit service were available.

Any overall examination of mortgage practices and problems should embody some consideration and thought about appraisals. I enjoy talking about appraisals because my experience as an appraiser has seen me trying to comply with some weird value definitions on one hand and, on the other, has found me attempting to ferret out exactly what an appraisal means. Fortunately, during the past few years there appears to be more reasonable and uniform thinking with regard to what is expected from an appraiser. There is, however, still considerable confusion in requirements by investors. The contemplation of appraisals raises the question of what constitutes price? What constitutes value? Should we ask the appraiser to make our decisions or have we the courage to make them ourselves? When thinking of real estate should we go along with those who say that the day of cycles is past? Can we agree with the school which maintains that our economy is such that there will never again be a depression in the real estate market? Should we ignore the vast industrial expansion which has occured during the past decade and a half? Can we believe that peaks and valleys in business activity can be controlled? Has the market for housing reached the saturation point? Shall we ignore the outlook for the tremendous population increase projected for the future? Shall we go along with those who say that we have reached a new plateau which is the start of a trend that will make us think of 1955 as a period of low living standards?

Each time we make an investment, these and many more questions face us. Every time we ask an appraiser to evaluate a piece of real estate he cannot help but contemplate these questions. Do we expect him to answer all of these questions? Do we ask him to take the price paid and justify it, or do we tell him to think back a few years and use this year or that as normal or do we ask him to inventory the facts as they exist at the time the report is made to assemble the data pertinent to the property and from this evidence report a reasoned fair market value? With this type of report we can then determine ourselves, whether the value supports a maximum loan. Too frequently we ask the appraiser to do two jobs in an appraisal report, that of reporting the value of real estate and that of underwriting the loan.

Relations with Appraisers

Our relationship with appraisers becomes simpler if we separate these two problems. If we do, the appraisal then becomes one of the tools used in making an investment. The competent mortgage loan officer recognizes this his problem consists of lending money which he expects to have returned with a fair rental for its use. He knows that he cannot use the appraisal alone as the basis for his investment for it has been demonstrated too often that such a practice is fraught with danger. The prudent mortgage investment calls for two sets of facts: one which deals with the security in the form of the real property and the other with the source of the income from which payments are to be made together with the economic factors which affect the durability and longevity of that income source. When dealing with residential property, some part of the householder's earnings throughout his lifetime always have and always will be dedicated to housing—call it what you wish, rent or mortgage payment.

We should accept the appraisal report for what it is, a conclusion supported with a compilation of data. This report, when combined with our own thinking as to the future worth of the dollar, an evaluation of world affairs, a summary of economic thinking concerning present and future

conditions should be the basis for our decision. It seems unreasonable to ask the appraiser to alter facts as they exist on a given date. It appears to be injudicious to ask him to "guesstimate" a value called long-term value, or stabilized value or mortgage value. They are all fictitious. We must realize that his ability to gaze into the crystal ball and forecast the future is no greater than our own. If the report gives a well reasoned fair market value estimate as distinguished from market price he has done all that can be justly expected of him. With such a report let us make our own economic adjustments and decide whether the property justifies a 10 per cent or a 66⅔ per cent loan. A good fair market value report will serve as an adequate guide at the time of liquidation if such is necessary. We cannot allow ourselves to be swayed by this report for it would be foolhardy to let it divert our attention from the overall underwriting problem.

What an Appraisal Should Be

Many have fooled themselves into expecting the appraiser to do for $10 or $50 or $500 what no one has ever been able to do with any consistency—forecast the future. Conservatism is an attribute but let us not misinterpret the term and read into it the necessity of disregarding fact. We have attempted to say that this or that is normal. None of us knows what normal means. Lending officers can be as conservative as they wish and still use factual appraisals. Loans do not have to be made at the full legal limit. Loans do not have to be made with the most favorable and liberal amortization terms. If the appraisal supplies the proper information, real service is done in guiding the investor toward sound limits and proper terms. Valuation of real property is an important part of risk rating procedure. Value of property and the ability of a borrower to repay a loan are different problems. Future economic swings and dollar values present still another set of problems. Let us keep them separate and ask the appraiser to report only on the property itself. The appraiser does not make value. His job is to report the reactions of intelligent and willing buyers and sellers when they meet in the market place. An appraisal that is 20 or 30 per cent below fair market value is just as unreliable as one which exceeds fair market value by the same amount, for neither gives a true picture of a very important segment of data required to do a good underwriting job. Let the investor make any adjustment he believes to be sound or expedient to the valuation report. It is the investor's responsibility to make decisions concerning the overall economic outlook just as it is when any other type of investment is purchased. It is the investor's responsibility to determine whether the people who constitute the market are wise or stupid and for how long.

Most correspondents are friendly souls. They like to have their investors visit their office periodically and examine the territory in which they are operating. They are anxious to get the reactions of investors to established and new areas within that territory. This association, at the point of operation, is beneficial to all; yet mortgage bankers tell me that some investors with whom they are currently doing business have not seen their office nor their investments over a period of years. Possibly this indicates that the investors have blind confidence in their agents. Maybe it is a rare compliment to their correspondent. It appears to be that it is not sound mortgage operation for I believe that intelligent analysis of applications far from the scene of operation requires constant on-the-spot review of the lending areas. Better understanding and mutual confidence must result from personal conference at the scene of local activity.

When a mortgage loan application is taken by a correspondent, good selling requires that the applicant be urged to sign the application and other forms at the point of agreement. Yet, frequently, the mortgage banker may, at this point, be in doubt as to which of his companies will match the mortgage. We all have our idiosyncracies and personal feelings on certain types of loans. The great majority of applications require pretty much the same information. The information required for a submission does not vary to a great degree, yet any mortgage banker representing more than one investor has complete sets of forms for each investor. It should not be too difficult for investors to get together and come up with some standard application. It is worth a real try and I am sure that the Mortgage Bankers Association would cooperate to its fullest capability. Again, it would effect some saving in cost, particularly at the retail level. We cannot afford to overlook any possibility.

If future performance in the life industry is to follow the past, we can anticipate a doubling of our assets during the next 10 to 12 years. If this is true and investors wish to maintain their present ratio of assets in mortgage loans, it will be necessary to increase mortgage loan portfolios 100 per cent during the period. The population expansion projected will undoubtedly produce the mortgages to do the job. Unfortunately, good mortgage men cannot be made in a few months. Now would be a good time to give some thought to the training of the man power necessary to adequately handle this business. Good personnel will be required both at the investor and correspondent level. Training this personnel is expensive and cannot be undertaken without some indication of future plans on the part of investors. Each company has its peculiar problem in portfolio management but I believe that we can give some indication to our correspondents of our future plans and desires. We investors should take advantage of the excellent School of Mortgage Banking sponsored by the Mortgage Bankers Association and of the appraisal courses sponsored by the American Institute of Real Estate Appraisers. They will give our interested people a firm foundation on which to build good mortgage management.

Eight Points to Remember

This report has been, in a sense, an introspection—the act of looking within. The examination has been brief. I have suggested that we in the life insurance industry give thought to eight points which might accomplish some betterment in mortgage investment:

» Better communication with our allies, the correspondent and the appraiser.

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What Does It Cost You

TO ORIGINATE A LOAN?
TO SERVICE A LOAN?

Do you know? A few say they do, others like to think that they do but far more recognize that they don't know their actual costs, certainly not in the same way manufacturing companies know their costs down to the last penny. Mortgage banking is the only large industry in the country that has no standardized system of cost accounting. Some pioneering work has been done in the field by a few companies but nothing is available today that meets the requirements of a reliable cost accounting procedure. This need has not gone unrecognized but, because of the nature of the mortgage lending operation, the task of developing a system has been a complicated one.

Now an effort has been started to accomplish something that is as important for our business as anything else at this time. Mr. DeYoung tells here what has been done so far, and he will have more to report in the months ahead. You will want to follow it closely as a recommended system materializes.

By EDWARD J. DeYOUNG

Assistant Director, MBA Servicing and Accounting Department

TWO most frequently asked questions in the mortgage banking industry are "What does it cost to originate a loan?" and "What does it cost to service a loan?" Of the two, the latter probably is asked more. But, in a business as diversified as mortgage banking, why should these two questions pertaining to costs be so predominant?

E. J. DeYoung

The answer is simple enough. The availability of cost data, relative to originating and servicing mortgage loans has been almost non-existent. It is true that a few mortgage bankers have determined these costs within their individual organizations for their own private use. Such results, however, are almost entirely worthless except to indicate an internal trend. Unless such cost information is obtained by using a standardized system, and then compared with other results obtained in a like manner, the resultant figures are meaningless. Except in rare instances, it is an established fact that absolute figures are of no value, until matched against comparative data.

A little more than a year ago, we in MBA's Servicing and Accounting Department realized that the constant flow of inquiries seeking cost figures could no longer be answered merely by heresay comments and unsubstantiated personal opinions. It was decided that the natural, and only, way to obtain satisfactory answers to cost questions was through the medium of cost accounting.

In our search for accurate cost figures, we first contacted the mortgage companies in an effort to discover which cost accounting systems were currently in use, and what cost data was available. The findings were not only extremely revealing but actually startling. We were amazed to learn that, but for those exceptions noted earlier in this article, all mortgage firms contacted either (1) had no conception whatsoever as to what cost accounting is; or, (2) had never utilized this form of accounting, and saw no need for its adoption in their business. In direct contrast, however, we found all companies to be interested in knowing their costs.

We next uncovered the equally startling fact that the mortgage banking industry is the only known nationwide business not employing—or at least not having available—a standardized system of cost accounting. We discovered that our MBA Headquarters Office is probably the only national association office not able to supply cost data to its members upon request.

After this preliminary investigation, the need for further and immediate work in the field of cost accounting within the mortgage industry was firmly established. Though the need for cost accounting research is thus generally apparent, not everyone may agree to our terming the situation "startling." However, it is startling that one of the nation's largest industries should be selling a product today without the remotest idea as to its cost.

Imagine one of our large automobile manufacturers placing one of its products upon the market without first knowing the exact cost of that product right down to the least important nut or bolt. Or, try picturing a large mail order house publishing its annual catalogue, containing several thousand items, with no idea whatsoever as to the exact cost of the items listed. Situations such as these sound ridiculous; but a great majority of mortgage bankers today are just that ridiculous in knowing neither the cost of doing business nor the cost of their product.

Many will defend themselves by contending that in the mortgage busjness the selling price of the product is not controlled by the seller, and therefore knowing the exact cost is irrelevant. In varied application, this is true of all businesses. In few industries is the cost of the product the sole determinant in fixing the price. Market conditions and competition are the forces that almost invariably fix the selling price of any product. Being aware of the exact cost, however, is of extreme importance in controlling what must be done in order to profitably sell at the current market price.

Before enumerating the various applications of cost accounting, and the attendant advantages to be gained from its use by the mortgage banker, some observations of cost accounting are in order. Innumerable definitions of cost accounting may be found in any text treating the subject. Actually, all accounting and financial recordkeeping is, in the true sense of the word, cost accounting. The already familiar accounting records such as ledgers, journals, balance sheets, income statements and year-end reports simply reflect income and expense which is accounting of costs and the reporting in difference between income and costs. Cost accounting, which is generally thought of as a separate and distinct field of endeavor, is merely a more detailed and precise extension and breakdown of the figures already contained in a company's regular accounting records. Beyond this, cost accounting holds no mystery.

Conversely speaking, however, cost accounting *per se* holds no magical formula for decreasing expenses or increasing profits. Viewed by itself, cost accounting is analogous to an exploratory medical X-ray. The X-ray does nothing to expressly cure the ailment, it merely locates and identifies the area in need of treatment. Thus it is with cost accounting, which is designed simply to pin point those individual operations of the over-all business most in need of remedial or corrective action.

Some may insist that cost accounting and the more advanced refinements of accounting systems are needed and are suitable for very large corporations but not for mortgage bankers, who are, for the most part, small organizations. We take issue with such thinking. Individually, many mortgage firms are small; collectively, however, they comprise one of the country's largest industries. Individual mortgage companies have experienced surprising growth in the past 20 years. With the continued expansion of the home building field, this individual company growth will undoubtedly continue. The many uncontrollable factors influencing the selling price of mortgages makes it imperative that the one controllable factor of cost be ascertained and handled accordingly. In addition, today's ever-increasing costs and small-unit profit make it more and more important to have exact working cost data. The conditions just mentioned could conceivably indicate that the smaller the company the greater the need for cost accounting, since the small firm is least able to withstand losses occuring in cost items.

There should exist no need for a persuasive program designed to convince business executives of the importance of readily available cost data. It should be obvious to all. In all types of industry and business the most successful and progressive companies employ cost systems and cost data on a regular basis. Since costs are almost the only remaining variables in today's business picture; they must be accurately identified if there is to be any control. The complexity of modern business, like flying, demands that it be performed with modern instruments, and not left to chance by attempting to "fly by the seat of one's pants."

Our everyday work reveals areas of operation with accompanying problems, where the techniques of cost accounting can provide true and immediate answers. Without exception, during every servicing consultation trip that we make, the question of just when is the proper time to transfer servicing from bookkeeping machines to electronic equipment is bound to arise. For some time now, mortgage bankers have been attempting to decide upon this point of transition, based on number of loans serviced, number of investors, type of loans and many other equally unreliable yardsticks. With an adequate cost system, the time for changeover would be focused to a precise time and point—thus leaving no room for doubt.

We know of one midwestern firm that has engaged a service bureau to handle their mortgage loan servicing. The volume of loans to be serviced, and the unit cost agreed upon, will result in a monthly charge to the mortgage company approximately one-third higher than what it would cost to rent its own equipment! In addition, by renting its own equipment, all other phases of the business could also be placed on that same equipment. And future growth could be accommodated without incurring additional expense. Several hundred dollars per month could be saved—if only this company had based its decision upon current cost accounting data.

Recently, a mortgage banker opened a branch office some distance from its established headquarters. Two or three million dollars worth of loans were originated, sold and servicing contracted for at one-half point, before this company discovered that all other firms in the area always received a three-quarters rate for servicing because of the average size loan and servicing difficulties peculiar to the area. Once again, competent cost

studies would have prevented this blunder and subsequent loss of revenue.

Last year we visited a commercial bank that was servicing a few hundred loans for an almost equal number of small investors. These loans were all paid down to an average loan balance of approximately $1,100. The servicing of these loans demanded an extremely disproportionate amount of time and expense when compared to the remainder of the bank's servicing portfolio. When it was suggested that these loans be repurchased, because continued servicing would prove unprofitable, management stated that though this had been considered, the holders of the loans wanted a premium for repurchase. A cursory cost analysis revealed that sufficient economy in servicing costs would result to warrant the repurchase of these loans, even at a premium. An established cost accounting system would have shown the exact dollar amount balance at which these loans became a loss item, and savings could have been made during the past several years on this group of loans.

There are, of course, hundreds of other specific examples that could be cited for the support of cost accounting and cost data. We are convinced of the necessity for, and the practicality of, cost accounting procedures for mortgage bankers.

The completion of our preliminary examination into the existing uses of cost accounting by mortgage bankers, as already noted, revealed a nearly complete dearth of cost analysis procedures in our industry. We, therefore, sought out the best accountants in MBA membership, a few of whom had already done some cost work within their respective companies. All agreed that the design and development of a standardized cost system applicable to all mortgage bankers was a very worthwhile undertaking. These men graciously volunteered to assist us in any way possible in creating a workable cost system.

Correspondence and personal meetings with those who had agreed to assist us took place for almost an entire year before we finally arrived at what we believe to be the desired result. In the interim several proposed cost systems were devised, and

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Something for Everybody in MBA's 1956 Program of Nation-wide Meetings

Never before has MBA staked out a busier schedule than has been projected for the first half of 1956—in fact, few if any national associations will bring their members together more frequently to discuss mutual problems than MBA will do. And before the schedule has been completed, just about everything having to do with mortgage lending and investing will get an airing sometime at someplace along the meeting highway. There's something for everybody in every type of firm in the 1956 program of meetings.

The first event, the MBA-NYU Senior Executives Conference, has just been completed with record attendance but still accommodating only about half of those who wanted to attend. Next follows the Chicago Conference. All in all, the program embraces:

>> A second Senior Executive Course at SMU, Dallas.

>> Mortgage Conferences in Chicago, New York, Atlanta and San Francisco.

>> Mortgage Clinics in Richmond, Albuquerque and Seattle.

>> Servicing Clinics in Chicago, Washington, D. C., Seattle and Nashville.

>> A Farm Mortgage Meeting in Chicago.

>> The Schools of Mortgage Banking at Northwestern and Stanford universities—the latter coming in July and August.

>> Then, reserved for the latter half of the year, is the annual Convention in Chicago, October 8-11.

The Conference and Clinic themes are pretty much the same, except that the programs of the former are somewhat more expanded. The Schools are, as all members well know, the one and only source to which those in the mortgage industry can turn for higher training in our field.

But the Servicing Clinics are new this year, and merit a special reminder to every member now. Those at the top management level turn to the MBA-NYU course (and soon to the companion SMU course in Dallas) for the opportunity to hear the broad trends of the economy discussed. These same management officials account for most of the attendance at the Conferences, Clinics and Convention. Now MBA has added something for those whose job it is to handle the servicing end. So here is an opportunity to do something for them that is sure to pay dividends in the type of performance they offer—send them to one of these one-day servicing clinics. There's no part of the business changing more rapidly than servicing, no branch where the changes of the past decade have been more pronounced. There is no place where new ideas and recent innovations offer greater prospect of an improved profit margin than right in your own office—through more economical and efficient servicing.

So, this is an excellent opportunity for you and your employees to profit from everything that has been developed within recent times. Don't overlook this valuable opportunity.

MBA Midwestern Mortgage Conference in Chicago Opens Heavy 1956 Schedule

The 1956 lead-off meeting is Chicago, usually competing with the New York Conference for the year's top regional registration. Among the many topics highlighting the Midwestern Mortgage Conference, Chicago, February 23-24, Conrad Hilton Hotel, will be one subject never before presented at an MBA meeting—"Management Succession in Small and Growing Enterprises." This address, of basic interest to all members, will be delivered by William A. Clarke, president, W. A. Clarke Mortgage Company, Philadelphia.

Following the address a panel discussion, moderated by Mr. Clarke, will analyze further the factors involved, and from a variety of viewpoints. Participating on this panel, in addition to Mr. Clarke, will be John F. Austin, Jr., MBA vice president, president, T. J. Bettes Company, Houston; Lindell Peterson, MBA president, president, Chicago Mortgage Investment Company; James W. Rouse, president, James W. Rouse & Company, Baltimore; Brown L. Whatley, president, Stockton, Whatley, Davin & Company, Jacksonville, Florida; S. Van Berschot, assistant treasurer, Continental Assurance Company, Chicago.

Featured speakers at the Conference will include King Upton, vice president, First National Bank of Boston; Albert M. Cole, administrator, Housing and Home Finance Agency, Washington, D. C.; George W. Mitchell, vice president, Federal Reserve Bank, Chicago; and G. Rowland Collins, dean, Graduate School of Business Administration, New York University.

Mr. Upton will discuss "Interim Financing of Closed Mortgages and Long Term Forward Commitments." The subject of Mr. Mitchell's address will be "Monetary Policy and Its Effect on Mortgage Financing." Dean Collins will analyze "The Economic Outlook."

Lindell Peterson, MBA president, and president, Chicago Mortgage Investment Company, will deliver the opening address of the Conference. He will speak on "The Mortgage Outlook."

"Washington News and Trends," will be discussed in an address by Samuel E. Neel, MBA general counsel, Washington, D. C. Mr. Neel also will serve as moderator for a panel discussion dealing with "Insured and Guaranteed Mortgages."

Panel participants will include H. Duff Vilm, H. Duff Vilm Mortgage Co., Indianapolis; W. W. Bunge, president, Amortized Mortgages, Inc., Milwaukee; James J. Flanigan, chief of operations, FHA, Chicago; Frank Shugrue, manager, mortgage section, Bankers Life Insurance Co. of Nebraska, Lincoln; Layard G. Thorpe, loan guaranty officer, VA, Chicago; Arthur W. Viner, national committee, Voluntary Home Mortgage Credit Program, Washington, D. C.

They Will Speak at Midwestern Mortgage Conference


Albert M. Cole


John F. Austin, Jr.


P. S. Bower


Arthur W. Viner


Frank J. McCabe Jr.


Brown L. Whatley


Wallace Moir


George Dovenmuehle


Dale C. Thompson


H. Duff Vilm


B. B. Bass


James W. Rouse

Another panel discussion, "Conventional Loans, Including Income Properties," will be moderated by B. B. Bass, president, American Mortgage and Investment Company, Oklahoma City. Joining Mr. Bass on the panel will be P. S. Bower, assistant general manager and treasurer, The Great-West Life Assurance Company, Winnipeg, Canada; George H. Dovenmuehle, president, Dovenmuehle, Inc., Chicago; Wallace Moir, MBA past president, president, Wallace Moir Company, Beverly Hills, California; Dale M. Thompson, president, City Bond and Mortgage Company, Kansas City, Missouri; Howard J. Tobin, vice president in charge of mortgage loans, The Northwestern Mutual Life Insurance Company, Milwaukee.

Others to speak include Robert H. Pease, vice president, Draper and Kramer, Inc., Chicago, who will discuss "The Research and Educational Trust Fund;" Peter V. Cloke, mortgage secretary, The Guardian Life Insurance Company of America, New York, who will undertake the "Shortcomings of the Correspondent in Mortgage Banking Operations"; and Frank J. McCabe, Jr., MBA assistant secretary-treasurer, Chicago, who will discuss "Make MBA a Partner in Your Business."

D. R. Beaumont, vice chairman, MBA Clinic Committee, president, D. R. Beaumont and Company, Chicago, will preside as general chairman of the Conference. B. B. Bass, Oklahoma City, is chairman of the Clinic Committee arranging the program.

Four Meetings Devoted to Servicing on Association's Program This Year

After several years of scheduling individual servicing sessions at various MBA meetings, this branch of the mortgage industry will come in for a full series of clinics this year, each devoted to nothing but the problems of servicing. The schedule is

>> Chicago, March 12, La Salle Hotel.

>> Washington, D. C., March 14, Hotel Statler.

>> Nashville, March 16, Andrew Jackson Hotel.

>> Seattle, March 17, Olympic Hotel.

The meetings have been organized under the general theme of "working together and coordinating efforts"; and while everyone now engaged in any phase of mortgage lending will find the programs of primary interest, it is those actually in the servicing and accounting departments who will derive the greatest reward.

So, in your plans to attend the MBA meetings during the first half of 1956, do not overlook the opportunity presented to you to send members of your servicing and accounting staffs to one of these four meetings.

Members in the individual areas served by these meetings will receive the actual programs well in advance. As an indication of the type of meetings they will be, however, here is a run-down of the opening Clinic.

W. James Metz, controller and director, MBA Accounting and Servicing division will preside, followed by an address by Thomas E. McDonald, vice president, T. J. Bettes Company, Houston, on "Management and Employees Are on the Same Team."

The remainder of the morning session will be devoted to "Problems of the Investor Which are Created by the Correspondent"—such topics as, Is the correspondent performing satisfactorily? Expense-cutting suggestions

for servicers. Investor audits are of little value. Implications of home owners' comprehensive insurance. Standards for adequate fidelity bond coverage.

Participating will be

Howard E. Meyer, Manager of Servicing, New York Life Insurance Company, New York.

John Leonard, superintendent of mortgage servicing, Mutual Life Insurance Company of New York.

L. C. Forth, mortgage office inspector, Sun Life Assurance Company of Canada, Montreal.

John K. Benoit, city loan office supervisor, Equitable Life Insurance Company of Iowa, Des Moines.

Louis J. Rub, assistant vice president, East River Savings Bank, New York.

Harvey D. Wilmeth, director of mortgage service and research, The Northwestern Mutual Life Insurance Company, Milwaukee.

At the noon luncheon, those attending will hear MBA President Lindell Peterson speak on the foundation of the investor-correspondent relationship. At the afternoon session, members will hear a talk by William I. De Huszar, treasurer, Dovenmuehle, Inc., on coordinating production and servicing activities. Following that, Edward J. DeYoung, MBA assistant director of accounting and servicing, will head a panel discussion on solutions to everyday operating problems. Participants include:

Richard E. Delaney, secretary-treasurer, Percy Wilson Mortgage and Finance Corporation, Chicago,

W. W. Dwire, vice president, Citizens Mortgage Corporation, Detroit.

John J. Griffin, Jr., vice president, General Mortgage Company of St. Louis.

R. M. Karns, vice president, Home Mortgage & Investment Co., Oklahoma City.

Farm Mortgage Clinic Precedes Chicago Conference in February

As a special added attraction at the Midwestern Mortgage Conference in Chicago, February 23-24, the MBA Farm Mortgage Committee, headed this year by Paul Mann of Wichita, will sponsor a special Farm Mortgage Clinic the day before, February 22. The initial effort along this line last year was highly successful, and it appears that the one coming up should be even better. It opens with a luncheon in the Hilton's Bel-Air Room. The speakers are

E. C. Johnson, Land Bank Service, Farm Credit Administration, Washington, D. C. giving a resumé of farm lending conditions.

F. E. Ferguson, manager of farm loans, Northwestern Mutual Life Insurance Co., Milwaukee, speaking on how an insurance company looks at farm loan applications.

A. D. Weber, Dean, Agricultural Department, Kansas State College of Agricultural and Applied Science, Manhattan, Kansas, speaking of the agricultural outlook.

So, for every mortgage man interested in the farm side of this business (and there are more of them than is generally appreciated), here is an opportunity to hear all that's new and significant in this branch of the business—and attend the Chicago Conference at the same time. All the farm meeting requires is a ticket to the luncheon and that's $4.

WHAT DOES IT COST?

(Continued from page 46)

then either abandoned altogether or revised and altered. The old saying that "accounting is not an exact science" was never more positively exhibited. Disagreement on agreement was the general rule of our progress. The constructive and critical comment by those assisting us proved to be extremely beneficial because it resulted in the best possible treatment of several controversial points within the cost system.

Late last summer we finally arrived at a cost accounting system for mortgage bankers. But, in order to achieve further refinement, we felt it would have to be tested in actual business operations. Forty companies were carefully selected for this purpose. All of those chosen were companies which we had personally visited at one time or another, and which we were certain had an individual on their staff who was capable and willing to cooperate with us on this project. As much care as possible was exercised in selecting firms of various sizes, type of operation and geographic location. Work sheets with accompanying instruction sheets were sent to these companies for calculating, entering and submitting to our office their actual income and expense figures for the most recent accounting period.

The results of this selected test were far better than even we had anticipated. No reluctance whatsoever was shown by the participating companies in making available to us their most confidential of operating figures. Also, as requested by us, many suggestions and recommendations were submitted. These will aid greatly in further improving the overall cost system.

Final tabulation and comparison of these cost figures is now being conducted, and the results will be published in a forthcoming issue of THE MORTGAGE BANKER. At that time, we will present also an explanation of this standardized cost accounting system, why certain items are treated as they are, and how the system is applied to practical operations. We will discuss, too, and comment upon, the actual cost figures as revealed in our sample cost study. To our knowledge, this will be the very first time that true and valid cost figures, which can be compared on an industry-wide evaluation scale, have ever been available.

Point of Origin: In this issue, Dr. Nourse first addressed the American Economic Association in New York, Dr. Adams the Michigan Bankers Association in Ann Arbor, Mr. Anderson the Life Insurance Association of America in New York and Mr. Shugrue the American Life Convention in Chicago.

O. J. Brichler Heads St. Louis MBA

O. J. Brichler, president, Shaw, Brichler & Coleman, Inc., was elected president of the St. Louis MBA to succeed John J. Griffin, Jr., vice president, General Mortgage Co. of St. Louis. The Association's new officers are, left to right, E. W. Hudspeth, vice president, Maginn-Martin-Salisbury, Inc., vice president; Wm. H. Byrne, secretary, Dolan Company, treasurer; Mr. Brichler; Mr. Griffin; and W. C. Rainford, president, Mercantile Mortgage Company, secretary. MBA President Lindell Peterson will address the Association at its March meeting.

John R. Womer Is Head Chicago MBA

John R. Womer, vice president, Great Lakes Mortgage Corporation, was elected president of the Chicago MBA to succeed Irvin R. Schildein, president, Quinlan and Tyson Mortgage Corporation, Evanston, at the Association's annual meeting. H. Hoyt Thompson, Ward Farnsworth and Co., was elected vice president and Martin O. McKevitt, The First National Bank of Chicago, secretary-treasurer.

Directors named for terms ending January, 1958, were Edward W. Asmus, Pullman Trust and Savings Bank; Merrill Bonnevier, Irvin Jacobs & Company; Theodore H. Buenger, Dovenmuehle, Inc.; Harry C. Eigelberner, Chicago Mortgage Investment Company; Jack N. Langworthy, Uptown Federal Savings and Loan Association; Robert H. Pease, Draper and Kramer, Incorporated; Herbert F. Philipsborn, H. F. Philipsborn & Co., and P. Warren Smith, Youngberg-Carlson Co.

Womar has been with Great Lakes Mortgage Corp. since 1935. During the World War II years, he served the Division of Defense Housing Coordinator in Washington, and he was on the staff of the adjutant general of the U. S. Army. He became a vice president of his firm in 1948.

The Chicago MBA annual meeting was in the nature of a tribute to MBA President Lindell Peterson who headed the local association in 1949. He was given a clock inscribed with a note of recognition for his service to the Chicago association and to MBA. He addressed the meeting briefly, predicting that, despite the problems confronting the mortgage industry in 1956 such as credit restrictions, the year would prove to be a good one for mortgage lenders, builders and home buyers.

Louis P. Wolfort Is Louisiana MBA Head

Louis P. Wolfort, executive vice president, Miller Mortgage Company, Inc., New Orleans, was elected president of the Louisiana MBA at the association's annual meeting. He succeeds Clarence A. Legendre, president, Standard Mortgage Corporation, New Orleans. John Dane, Jr., Dane & Northrop, New Orleans, and Tyler Bland, vice president of Rapides Bank & Trust Company in Alexandria, were elected vice presidents. Lloyd Adams was re-elected secretary-treasurer.

Governors elected were W. W. Baltar, Jr., Ralph W. Baucum, T. Hendon Blaylock, Gustave C. Gehr, Raymond E. Kron and Darwin G. Nichols.

MBA President Lindell Peterson addressed the meeting on the mortgage outlook and MBA General Counsel Samuel Neel spoke on Washington affairs. W. James Metz, MBA director of accounting and servicing, spoke on servicing.

E. F. Striepeke Is Pittsburgh Head

E. F. Striepeke, assistant trust officer, Commonwealth Trust Company of Pittsburgh, was elected president of the Pittsburgh MBA. Walter A. Scott, Jr. of Scott and McCune, Inc. was elected vice president and J. Paul Krome, secretary, Provident Trust Company, secretary-treasurer.

Lubbock MBA Sets Up Scholarship

The Lubbock, Texas MBA has established a scholarship fund at the Texas Technological College in Lubbock, proceeds of which are to be awarded annually to a junior or senior student majoring in finance. The aim is to assist the student with his college education as well as to publicize mortgage banking in an effort to encourage students to enter the industry, according to R. Miller Hicks, Association president.

C. Edgar Smith Is Baltimore President

C. Edgar Smith, Merchants Mortgage Company, Baltimore, has been elected president of the Baltimore MBA. Leslie S. Wilson, W. Burton Guy & Company, has been elected vice president and Gordon Lee Smith, S. L. Hammerman Organization, Inc., has been elected secretary.

H. B. Thompson Is Phila. MBA Head

H. Bruce Thompson, president, Colonial Mortgage Service Company, has been elected president of the Philadelphia MBA; Joseph J. Braceland, vice president, Philadelphia Saving Fund Society, vice president; William K. Brandt, vice president, Central-Penn National Bank, secretary; and David Bloom, manager of mortgage department, Jackson-Cross Company, secretary.

Those elected to the board of governors for terms expiring December 1956 are David Solms, executive vice president, Eastern Mortgage Service Co.; Oliver S. Twist, vice president and title officer, Frankford Trust Co.; J. H. Latimer, Redding & Latimer; and T. Irving Howe, assistant vice president, Tradesmens Bank & Trust Co. Those elected for terms expiring December 1957 are J. L. Aylsworth, Jr., president, Mortgage Associates, Inc.; Raymond Gleadall, vice president, Home Life Insurance Co. of America; Edward J. Thomas, vice president, Saving Fund Society of Germantown, and Fred A. Werner, president, Lansdowne Federal Savings & Loan Association. Those elected for terms expiring December, 1958 are John Chatley, Jr., vice president, Fidelity Philadelphia Trust Co.; Joseph N. Gorson, president, Fidelity Bond and Mortgage Co.; Edward L. Stanley, associate manager of mortgage department, Provident Mutual Life Insurance Co.; and J. Elwell Whalen, president, Peoples Bond and Mortgage Co.

D. K. Vanneman Is Atlanta MBA Head

Donald K. Vanneman, president of Etheridge & Vanneman, Inc., has been elected president of the Atlanta MBA, succeeding Jack Adair, president of Adair Realty & Loan Company. Mr. Adair has been elected president of the Atlanta Real Estate Board for 1956.

D. K. Vanneman

Other officers elected were James G. Hardy, Jr., executive vice president, Spratlin, Harrington & Thomas, Inc., vice president; Edgar P. Farrell, vice president, Adair Realty & Loan Company, secretary-treasurer. C. D. LeBey, president, C. D. LeBey & Co., and Frank C. Owens, president, Draper-Owens Co., were elected to the board of directors to serve with Thomas V. Cauble, manager, Mortgage Loan Department, Adams-Cates Company; John S. Schneider, manager, D. L. Stokes & Co., Inc.; Rankin-Whethers Realty Co.; Carey Hooks, Roy D. Warren Company, Inc.; and Mr. Adair.

Robert Tharpe, president, Tharpe & Brooks, as chairman of the committee for the MBA Southern Mortgage Conference to be held in Atlanta April 7-10, 1956, introduced the guest speaker, Frank J. McCabe, Jr., MBA assistant secretary and treasurer, who came from Chicago to discuss plans for the meeting which will bring to Atlanta mortgage bankers and investors from all over the country. Mr. McCabe complimented the local association on the work already done towards the success of this important meeting.

M. R. West, Jr., Heads Washington MBA

Martin R. West, Jr., vice president, Weaver Bros., Inc., was elected president of the Metropolitan Washington, D. C. MBA and William F. Bergmann, vice president and treasurer, Arlington Realty Company, Inc., was elected vice president. Other officers named are Frederick X. Wilson, vice president, Suburban Trust Company, treasurer; Frank S. Hight, Jr., vice president, Bogley, Harting & Hight, secretary; and H. Loy Anderson, vice president, Walker & Dunlop, Inc., general counsel.

Governors named include Roger W. Hatch, vice president and treasurer, Walker & Dunlop, Inc.; A. Britton Browne, Jr., secretary, Randall H. Hagner & Company, Inc.; Samuel E. Bogley, president, Bogley, Harting & Hight and Francis C. Little, senior vice president, B. F. Saul Company.

Mr. West is one of the younger members in the mortgage banking industry in the capital district, and a graduate of Princeton.

The Association is now in its third year and has 43 member firms, including all local mortgage bankers and life insurance companies as well as many banks.

In the photo taken at the first board meeting are shown, seated left to right, Mr. Wilson, Mr. Bergmann, Mr. West, Jr., Mr. Hight, Jr. and Mr. Anderson. Standing, left to right, are Mr. Hatch, Mr. Browne, Jr., Mr. Bogley and Mr. Little.

President Peterson's Speaking Engagements

January 26, Philadelphia MBA

February 6, Indianapolis MBA

March 1, California MBA, Coronado

March 22, St. Louis MBA

April 16, Iowa MBA, Fort Dodge

Frank P. Leslie, chairman of the board, Title Insurance Company of Minnesota, announced the election of **Leo A. Reuder** as president, succeeding **J. F. Horn** who has retired after serving as president for eleven years. The growth of the Company under Mr. Horn has been one of the best business stories of Minneapolis. Each year during his presidency, the territory covered in the title insurance business has grown from state to state until the institution now covers twenty states. Total dividends paid to stockholders reached an all time high last year. Reuder has been with the Company since 1919 and is one of the leading title men of the country.

Paul P. Swett, Jr., formerly vice president of Baltimore Life Insurance Co. and now an independent financial consultant, and **William Elliott,** president of the Philadelphia Life Insurance Co., are among a group of private investors who have acquired a majority stock control of Maryland Life Insurance Co. They were represented in the transaction by the investment banking firm of Alex. Brown & Sons.

Waldo E. Francois has been named assistant treasurer and manager of the mortgage loan department of Pan-American Life Insurance Company, New Orleans. He joined the Company in 1929 as a member of the investment department . . . **Lloyd M. Bell** has been named assistant vice president of the Rapides Bank & Trust Company in Alexandria, Louisiana. He has been with the institution since 1948, starting as a mortgage loan field representative and becoming loan supervisor in the mortgage loan department in 1952.

The Mutual Benefit Life Insurance Company, Newark, honored **Irvin Jacobs,** president, Irvin Jacobs & Company, Chicago, with a plaque attesting to his ten years' association with the Company as mortgage loan correspondent.

The Jacobs Company, established 31 years ago, serves Mutual Benefit as correspondent in the northern portion of Illinois, southeastern Wisconsin, northwestern Indiana and western Michigan.

At the ceremonies at the home office, left to right are **Robert E. Smith,** second vice president and associate manager, city mortgage and real estate investment department; **Paul A. Nalen,** vice president and manager, city mortgage and real estate investment department; Mr. Jacobs; and Mutual Benefit's financial vice president, **Milford A. Vieser.**

J. E. Foster, Jr. has been elected chairman of the board of J. E. Foster & Son, Inc., Fort Worth, **Alvin E. Soniat** has been elected president and **Pat L. Davis,** executive vice president.

John D. Abbott has been named chairman of the board of Abbott Mortgage Co., Pittsburgh, and **Robert L. Cashion,** formerly with Mellon National Bank and Trust Co., has been named president.

Obituary

Seth H. Morford, 84, founder and chairman of the board of Burwell & Morford, Inc., Seattle, died in a Seattle hospital after a brief illness. Mr. Morford headed the firm for 56 years and lived in Seattle since 1887. Active direction of the firm in recent years has been under Kenneth J. Morford, his son, a member of the MBA board of governors.

CORRESPONDENTS-INVESTORS

(Continued from page 43)

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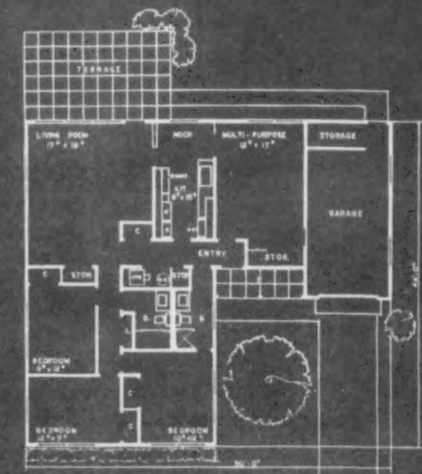

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5

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